Griffith Business School

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Doctor of Philosophy

By

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CORPORATE GOVERNANCE AND FIRM PERFORMANCE IN KUWAIT

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Abstract

This thesis examines the link between corporate governance and firm performance in Kuwait. Corporate governance—the framework that defines the relationship between shareholders, management, the board of directors, and other stakeholders—is an important element associated with monitoring, evaluating, and improving firm performance around the globe. In turn, firm performance is one of the most critical considerations for firms and their relations with stockholders and stakeholders, and therefore, for societal, financial, and economic wellbeing.

Good corporate governance is important everywhere, not least in Kuwait. Despite being a relatively small economy, Kuwait plays a leading economic and financial role in the Gulf states, particularly during the recovery stage of the Middle East revolutions of the early 21st century and following its own occupation during the First Gulf War in 1990–1991. Recently, Kuwaiti firms have also been subject to an extensive program of privatisation and market deregulation, aimed at very quickly stimulating stock market activity, assisting economic development and recovery, and facilitating international financial and economic integration.

However, Kuwait is unique in that it has very much lagged most other neighbouring markets in terms of capital market regulation and the development of corporate governance codes and guidelines. For example, unlike Bahrain, the United Arab Emirates (UAE), Oman, Saudi Arabia, and Qatar, Kuwait lacks comply-or-explain provisions in its guidelines. Further, unlike Bahrain and the UAE with their separate corporate governance codes and guidelines for banks and insurance companies, state-owned enterprises, real estate companies, and small-and-medium-sized enterprises, Kuwait’s early efforts at reforming corporate governance have largely only concerned banks. Kuwait is also interesting in a corporate governance context given the high level of family (including the House of Al-Sabah, Kuwait’s ruling royal family) and state ownership of publicly listed firms.

This thesis employs a mixed methodology, including both quantitative analysis for responding to the first of three research questions and qualitative analysis to respond to a fourth research question. The quantitative analysis primarily comprises a regression-based approach that specifies the returns on assets (ROA) and equity (ROE) and Tobin’s Q
(TQ) as dependent measures reflecting firm performance and corporate governance factors, including the board of directors, audit committee, and ownership structure as independent variables.

In the first research question, the nature of the relationship between ownership structure and firm performance in Kuwaiti industrial and services firms is explored. The sample comprises all Kuwaiti industrial and services firms listed on the Kuwait Stock Exchange over the period 2010–2017. The full sample period comprising 520 firm-year observations is divided into three time periods corresponding to the three separate corporate governance code regimes in Kuwait: a pre-corporate governance code regime (2010–2012) and a voluntary corporate governance code regime (2013–2015), both with 246 firm-year observations, and a compulsory corporate governance code regime (2016–2017) with 130 firm-year observations. Dummy variables identify each regime in the regression analysis.

The findings indicate that ownership structure plays a significant role in determining firm performance. According to ownership types in Kuwait (family, foreign and local institutional, and government ownership), family ownership and institutional local ownership appear to have the most significant influence on firm performance, both in terms of their impact on individual firms and marketwise due to the overall extremely high level of family ownership in the Kuwaiti market. In contrast, institutional foreign ownership is only associated with significantly lower levels of firm performance and only slightly higher levels of undervaluation. The findings for institutional local shareholdings show a high positive relationship with ROA, ROE, and TQ, which may reflect their familiarity with the local investment market.

In the second and third research questions, the nature of the association between board of directors’ characteristics, audit committee characteristics, and firm performance in Kuwaiti industrial and services firms is considered. The sample again comprises all Kuwaiti industrial and services firms listed on the Kuwait Stock Exchange over the period 2010–2017. The results reveal that board size positively relates to firm performance as expected, particularly in relation to the TQ. Also, the proportion of independent board members positively relates to ROA, ROE, and TQ, whereas the number of board meetings affects all of them.

The qualitative analysis draws on extensive semi-structured interviews conducted with the chairpersons, general managers, and financial managers of selected Kuwaiti industrial
and services firms in 2018. This provides detailed information about corporate governance processes within those firms to respond to the final research question about how cultural, social, political, and economic circumstances play a role in modifying the relationship between corporate governance and Kuwaiti firm performance. The results provide particularly interesting insights into how good corporate governance improves firm performance in Kuwait, including fostering trustworthiness, attracting foreign investors, increasing financial reporting quality, and raising the expectations of management quality. Several cultural and external factors modify the relationships between corporate governance and firm performance in Kuwait, including the recent Middle East revolutions and the adoption of International Financial Reporting Standards. The thesis contributes to the existing literature by adding knowledge about the corporate governance–firm performance relationship in Kuwait, including simultaneously investigating several dimensions of corporate governance, such as those relating to the role of boards, internal committees and processes, and firm owners. The thesis also provides Kuwaiti regulators and policymakers with important insights into the gains from good governance in Kuwaiti firms and the ways this may be achieved, and rigorous evaluation of different empirical frameworks and methods in quantitatively and qualitatively assessing corporate governance and firm performance, both in Kuwait and elsewhere.
Statement of Original Authorship

The work contained in this thesis has not been previously submitted to meet requirements for an award at this or any other higher education institution. To the best of my knowledge and belief, the thesis contains no material previously published or written by another person except where due reference is made.

Signature: [signature]

Date: ___ July 2020__________
Acknowledgements

IN THE NAME OF GOD: FOREVER EMPATHETIC AND GIVING, AND FOR PROVIDING US WITH SCIENTIFIC STUDY, SO WE COULD LIGHT THE WORLD.

It is here, after the writing of my thesis, that I would like to take the opportunity to thank every individual who has played a part in its creation. Truly, I would not have been able to embark on this journey without these people behind me.

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To my mother and father, for offering me a solid foundation upon which I have been able to comfortably construct the rest of my pursuits. You always keep me in your thoughts and prayers, and I will forever do the same for you.

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I would also like to thank professional editor, Robyn Kent1 and Kylie Morris, who provided copyediting and proofreading services according to university-endorsed guidelines and the Australian Standards for Editing Practice – Standards D and E for editing research theses.

1 Robyn Kent is RAK Editing Services, Accredited Editor (AE), Institute of Professional Editors (IPEd) and a professional member of Editors Queensland.
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May Allah bless you all.

Abdullah Alajmi, 2020
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<td>AEX</td>
<td>audit committee expertise</td>
</tr>
<tr>
<td>AIN</td>
<td>audit committee independence</td>
</tr>
<tr>
<td>AMT</td>
<td>audit committee meetings</td>
</tr>
<tr>
<td>SZE</td>
<td>firm size (Chapter 5)</td>
</tr>
<tr>
<td>AST</td>
<td>firm size (Chapter 6)</td>
</tr>
<tr>
<td>ASZ</td>
<td>audit committee size</td>
</tr>
<tr>
<td>AUD</td>
<td>Australian dollar</td>
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<tr>
<td>BIN</td>
<td>board independence</td>
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<tr>
<td>BMT</td>
<td>board meetings</td>
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<tr>
<td>BOU</td>
<td>board outsiders</td>
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<tr>
<td>BSZ</td>
<td>board size</td>
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<tr>
<td>COM</td>
<td>Compulsory Corporate Governance Code</td>
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<tr>
<td>CBK</td>
<td>Central Bank of Kuwait</td>
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<tr>
<td>CEO</td>
<td>chief executive officer</td>
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<tr>
<td>CFO</td>
<td>cash flow from operating activities</td>
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<td>CMA</td>
<td>Capital Markets Authority</td>
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<td>CSR</td>
<td>corporate social responsibility</td>
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<td>DTE</td>
<td>debt-to-equity ratio</td>
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<td>FAM</td>
<td>family ownership</td>
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<td>GDP</td>
<td>gross domestic product</td>
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<td>GOV</td>
<td>government ownership</td>
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<td>IFRS</td>
<td>International Financial Reporting Standards</td>
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<td>IMF</td>
<td>International Monetary Fund</td>
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<td>ISF</td>
<td>institutional shareholders foreign</td>
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<tr>
<td>ISL</td>
<td>institutional shareholders local</td>
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<tr>
<td>KD</td>
<td>Kuwaiti dinar</td>
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<td>KPC</td>
<td>Kuwait Petroleum Corporation</td>
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<td>KSE</td>
<td>Kuwait Stock Exchange</td>
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<td>LEV</td>
<td>leverage ratio</td>
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<tr>
<td>MENA</td>
<td>Middle East and North Africa</td>
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<td>OECD</td>
<td>Organization for Economic Co-operation and Development</td>
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<td>OLS</td>
<td>ordinal least squares</td>
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<td>PACI</td>
<td>Public Authority for Civil Information</td>
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<td>FP</td>
<td>firm performance</td>
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<td>ROA</td>
<td>return-on-assets</td>
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<td>return-on-equity</td>
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<td>SUB</td>
<td>firm subsidiary</td>
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<td>Tobin’s Q</td>
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<td>UK</td>
<td>United Kingdom</td>
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<td>UAE</td>
<td>United Arab Emirates</td>
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<td>USA</td>
<td>United States of America</td>
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<tr>
<td>VOL</td>
<td>Voluntary Corporate Governance Code</td>
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<tr>
<td>VIF</td>
<td>variance inflation factor</td>
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List of Research Outputs

During the period of PhD candidature, several research outputs were produced to disseminate concepts and results from the work undertaken by the candidate. The full list of these outputs is as follows:

**Journal Articles**


**Conference Papers**


Acknowledgement of Papers Included in the Thesis

Section 9.1 of the Griffith University Code for the Responsible Conduct of Research ("Criteria for Authorship"), in accordance with Section 5 of the Australian Code for the Responsible Conduct of Research, states:

To be named as an author, a researcher must have made a substantial scholarly contribution to the creative or scholarly work that constitutes the research output, and be able to take public responsibility for at least that part of the work they contributed. Attribution of authorship depends to some extent on the discipline and publisher policies, but in all cases, authorship must be based on substantial contributions in a combination of one or more of:

- conception and design of the research project
- analysis and interpretation of research data
- drafting or making significant parts of the creative or scholarly work or critically revising it so as to contribute significantly to the final output.

Section 9.3 of the Griffith University Code ("Responsibilities of Researchers"), in accordance with Section 5 of the Australian Code, states:

Researchers are expected to:

- offer authorship to all people, including research trainees, who meet the criteria for authorship listed above, but only those people
- accept or decline offers of authorship promptly in writing
- include in the list of authors only those who have accepted authorship
- appoint one author to be the executive author to record authorship and manage correspondence about the work with the publisher and other interested parties
- acknowledge all those who have contributed to the research, facilities or materials but who do not qualify as authors, such as research assistants, technical staff, and advisors on cultural or community knowledge. Obtain written consent to name individuals.

Included in this thesis are co-authored papers with other researchers. The signatures below signify the willingness of all co-authors for the paper to be included in the thesis. The current reference details (including publication status) for these papers are:
Chapter 5:

(Signed) ___________________________ (Date)

Candidate: Abdullah Alajmi

(Countersigned) ___________________ (Date)

Supervisor: Andrew C Worthington

Chapter 6:
Alajmi, A. and Worthington, A. C. "Board of directors, audit committee characteristics and firm performance", under editorial review at *Managerial Finance*.

(Signed) ___________________________ (Date)

Candidate: Abdullah Alajmi

(Countersigned) ___________________ (Date)

Supervisor: Andrew C Worthington

Chapter 7:
Alajmi, A. and Worthington, A. C. "Qualitative Insights Into Corporate Governance Reform, Management Decision-Making, and Accounting Performance: Semi-Structured Interview Evidence", under editorial review at *Qualitative Research in Accounting and Management*.

(Signed) ___________________________ (Date)

Candidate: Abdullah Alajmi

(Countersigned) ___________________ (Date)

Supervisor: Andrew C Worthington
Chapter 1: Introduction

1.1 Thesis Background

Corporate governance is an integrated system comprising practices, rules, and processes used to increase the quality of firm control and, thereby, firm performance by matching the interests of the firm’s shareholders, managers, clients, traders, creditors, and government. In so doing, corporate governance provides an essential framework for decreasing agency conflicts between shareholders and management within firms, in turn encouraging the efficient use of resources and accountability for the stewardship of these resources.

In terms of a formal definition, Shleifer and Vishny (1997) considered corporate governance to be a group of systems providing for potential external capital givers to earn a justified investment return, while the Organization for Economic Co-operation and Development (OECD, 2001) defined it as:

[T]he private and public institutions, including laws, regulations, and accepted business practices, which together govern the relationship in a market economy between corporate managers and entrepreneurs (corporate insiders) on one hand, and those who invest resources in corporations, on the other. (p. 13)

Elsewhere, Cadbury (2000) defined corporate governance as that:

[C]oncerned with holding the balance between economic and social goals, and between individual and communal goals. The governance framework is there to encourage efficient use of resources, and equally to require accountability for the stewardship of those resources. The aim is to align [as closely] as possible [with] the interest of individuals, corporations, and society. The incentive to corporations is to achieve their corporate aims and to attract investment, [and] the incentive for the state is to strengthen their economies and discourage fraud and mismanagement. (p. vi)

Corporate governance is therefore an important way to lead to better firm performance through improvements in firm operations and behaviour. This includes assisting the firm to avoid mismanagement, helping the firm to make timely improvements, providing shareholders with in-depth information about the business that promotes confidence in the business, providing sufficient disclosures that enhance the information about the firm
that users use to make correct decisions, preventing unethical behaviour, and consulting with different groups of stakeholders and managers on their interests.

Most firms around the world now focus on good corporate governance. The benefits are clear. Good corporate governance allows firms to control themselves more efficiently, to increase their access to capital, and reduce risk and protect stakeholders. It also helps simplify the board’s role in business strategy and helps ensure the firm’s directors have the information that they require by shaping and building an effective governance infrastructure. Finally, good corporate governance also assesses board and director performance and provides opportunities for improvements in firms in the future. Overall, good corporate governance helps firms, industries, and economies function better to the benefit of shareholders and stakeholders.

Companies in different countries, however, operate in different cultural, legal, social, and economic environments, leading to the development of different corporate governance systems. It is therefore important to understand the features of corporate governance in each country, and how these may change as a means of further improving firm performance. A comparison of the design and effects of different corporate governance systems in one or more countries can also assist with the optimal design of these systems in other countries.

Unfortunately, while there is abundant research on many of these issues in the well-developed markets and regulatory regimes found in advanced economies, this is lacking in nearly all developing economies. This is important, because the marginal gains to good governance that flow from ownership structure and the regulation within which it operates are much larger in these economies, and thereby have the potential to be more influential in improving company and economic performance, and with them, shareholder and stakeholder wellbeing.

1.2 Thesis Significance

The current PhD thesis rationale can be seen when considering various factors. The informational environment in Kuwait is believed to be far less rich and diverse than that in developed countries, such as the UK and the USA, with very little research effort directed towards understanding corporate governance and firm performance in the country. Nonetheless, Kuwait is not unimportant in this regard, with its stock market considered one of the most developed markets of the countries included in the Gulf
Cooperation Council (GCC). Accordingly, the study supports efforts centred on filling the void in the literature concerning corporate governance assessment in Kuwait.

Few studies have been completed in the GCC business environment to investigate the impact of corporate governance on firm performance. Therefore, this study focuses on Kuwaiti industrial and services firms since Kuwait is one of the fastest growing worldwide economies. In the last two decades, the Kuwaiti Government has paid more attention to supporting and developing good corporate governance mechanisms to increase investor assurance and encourage market enhancement and development. This study, in line with its methodology, provides experiential evidence from Kuwaiti industrial and services firms pertaining to the impacts of corporate governance on a typical firm’s performance measures.

Kuwait is recognised as unique among the Arab Gulf countries and is seen to offer an attractive marketplace in the region, primarily because it provides several opportunities for more investment. This study also considers stakeholders in recommending the appropriate firm structure, the benefit of distinguishing between firms with operative and inoperative corporate governance procedures, determining the exact meaning of operative and inoperative corporate governance, revealing the impacts of corporate governance on firms’ performance, the growth of awareness of agency theory and its relationship with corporate governance, and demonstrating the nature of the Kuwaiti stock market.

This study is recognised as different from prior studies, which have focused on developed countries such as Australia, the USA, and the UK. Nowadays, there is a growing awareness in line with the theories stemming from developed countries that could have limited adoption and may not find their system in developing countries, and Kuwait is seen to be one of them. Several differences have been identified in terms of the nature, way, size, and procedures of operation pertaining to the association between developing and developed financial markets, according to variances in their economic, cultural, social, and regulatory frameworks and marketplace behaviour (Ahunwan, 2003; Alanezi, 2009).

Few studies have been completed so as to investigate the relationship between corporate governance and firm performance in Arab Gulf countries (Abdallah & Ismail, 2017; Dalwai, Basiruddin, & Abdul Rasid, 2015; Zeitun, 2014); therefore, little information is available in relation to the roles of corporate governance mechanisms in these countries, and there is a significant need for such theories to be tested in the context of developing
countries, such as Kuwait, which is recognised by its diverse political, cultural, economic, institutional, social, and other issues.

Kuwait, as an emerging market, is deemed a unique case study to investigate the relationship between corporate governance and firm performance for several reasons. First, Kuwait delivers an exclusive natural setting for examining corporate finance theories because of the straightforwardness of the Kuwaiti tax system, which encompasses no personal taxes or corporate taxes. This system is totally different from that of developed and developing countries, which impose personal and corporate taxes. Accordingly, the Kuwaiti tax system could lead to different empirical results compared with other studies. Second, the continuing improvement underpinning the financial market has become important in terms of accelerating Kuwait’s economic growth, particularly following the Middle East revolutions recovery stage. More recently, several economic systems adopt by Kuwaiti industrial and services firms, for example through privatisation (process of deregulation). This adoption helps Kuwaiti firms to stimulate activity in the stock market, recover corporate governance and economic development, and adopt international integration. Finally, the Kuwait Stock Exchange (KSE) is the second-largest market in the Arab Gulf countries, yet remains without a capital market authority. In this regard, the impact of corporate governance on firm performance is important in terms of providing decision-makers and regulators in Kuwaiti industrial and services firms with in-depth information to allow them to avoid financial performance error and mistakes in the future, and accordingly develop their system to be covered by capital market authorities.

There has been a significant increase in the Kuwait stock market since it first started with just 30 listed firms in 1984, and with more than 200 listed firms currently listed (Alanezi, 2006) is recognised as another significant factor leading to the need to conduct this study. Several recommendations will be provided to decision-makers in line with enhancing and developing financial reporting in Kuwait. Furthermore, governance in Kuwaiti industrial and services firms comprises an exclusive ownership structure with an important level of

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2 Capital Market Authority “…defined as an independent body that supervises trading procedures, monitors transactions, and detects conflict of interest. It also can resolve conflicts between investors and companies, enhance transparency of information, regulate takeover and merging operations, and penalize illegal activities” (Al Mutairi et al., 2012, p. 597).
royal family ownership and substantial family ownership, which is totally different from that of Arab countries in the Middle East.

1.3 Thesis Motivation

Although Kuwait is only one of several emerging markets in the Gulf, it offers a unique case to investigate both corporate governance and the purported relationship between corporate governance and firm performance. First, Kuwait is a natural setting for testing corporate finance theory due to the straightforwardness of its tax system, having no personal or corporate taxes. This is quite different from nearly all other developed and developing countries. Kuwait is also unique in that there are substantial levels of royal and other family ownership, which is again vastly different from other Arab countries in the Middle East.

Second, the continuing improvements underpinning its financial markets have become important in terms of accelerating Kuwait’s economic growth, particularly in the recovery stage of the Middle East revolutions of the early 21st century and following its occupation during the First Gulf War in 1990–1991. Even more recently, Kuwaiti firms have been subject to an extensive program of privatisation and market deregulation, helping to stimulate stock market activity, mend corporate governance, assist economic development and recovery, and facilitate international financial and economic integration very quickly.

Yet, despite spectacular market developments, Kuwait is a relative latecomer to a general corporate governance code and guidelines. Although these are now broadly in place throughout the Gulf, and date from as early as 2002 in Oman, Kuwait only adopted them in 2013. This closely followed the establishment of its first capital markets authority in 2010 and revisions in 2016 to its Company Law to overcome weakness and gaps in existing capital market law and conduct. Nonetheless, Kuwait lagged many other Gulf countries in the administration of its corporate governance guidelines. For example, unlike Bahrain, the UAE, Oman, Saudi Arabia, and Qatar, Kuwait lacks comply-or-explain provisions in its guidelines. Furthermore, unlike Bahrain and the UAE with their separate codes and guidelines for banks and insurance companies, state-owned enterprises, real estate companies, and small-and-medium-sized enterprises, Kuwait’s early efforts largely only concerned banks.
Firms listed on the KSE are subject to two newly introduced and major sets of regulations: the CMA laws introduced in 2010 to regulate the behaviour of market participants (and which are not the subject of this analysis), and the company (or ministry) law implemented in 2016. These laws imposed many corporate governance articles and provisions obliging all listed companies to make necessary changes in their bylaws and internal policies. These include, among other items, a minimum number of board members, the required separation of the role of chair of the board and chief executive officer, the required presence of independent directors, and limits on the membership of other boards, especially those of competing companies. The articles also include restrictions on the disclosure of confidential information, and the banning of business and financing deals by board members, executive management, and their families with the company without the approval of the general assembly of shareholders.

The logical hypothesis is suggested a positive effect on the quality of corporate governance, and thus, on listed firm performance in Kuwait. However, the Kuwait Capital Markets Authority imposed the staged introduction of these provisions. Prior to 2013, there was no corporate governance code or guidelines; from 2013 until 2015, there was voluntary compliance with the code and guidelines; and from 2016 onwards compliance was to be compulsory. Consequently, this thesis examines not only whether firm performance has improved, but also whether the foreshadowed shift to a formal corporate governance code and guidelines, and within that, from a voluntary to a compulsory regime, entailed differing impacts on firm performance.

1.4 Aims and Objectives

The essential purpose of this thesis is to analyse four complementary objectives concerning corporate governance and firm performance in Kuwait. These aims are clustered in two groups. The first group has three aims: investigating the impact of board of directors’ characteristics, audit committee characteristics, and ownership concentration on firm performance in Kuwaiti firms to determine which of the corporate governance factors has more effect on firm performance in Kuwaiti firms. These three aims have been achieved in empirical results in Chapters 5 and 6 (quantitative method). The second group has one aim that is focused on determining the influence of immeasurable issues, such as cultural factors, religion, legal system, and political and economic circumstances, on the relationship between corporate governance and firm performance in Kuwaiti industrial
and services firms. To accomplish these objectives, four questions were established (see Section 1.5).

In addition, this study focuses on examining the association between board of directors’ characteristics (board size, board meetings, board independent, and board outsider), audit committee characteristics (audit committee size, audit committee meetings, audit committee independence, and audit committee expertise) and firm performance proxies (ROA, ROE, and TQ). The board of directors’ key purpose is to ensure the firm’s prosperity by collectively directing the firm’s affairs, while meeting the appropriate interests of its shareholders and stakeholders. The board sets long-term aims for firms that manage their upcoming direction. These aims are recognised during the voting period, whether quarterly or annual meetings. Periodically, therefore, the board must check whether these aims have been met or not. The existence of a strong board of directors enhances several issues in the firm environment, such as increasing the shareholders’ trustworthiness, overseeing, and controlling managers’ work, and protecting management from taking extreme compensation, to ensure that each party in the firm structure works within their scope. By achieving these issues through existing strong corporate governance, the quality of the firm will be increased, which means high firm performance.

1.5 Research Questions

The purpose of this thesis is to analyse four separate but related research questions concerning corporate governance and firm performance in Kuwait. Together, these shed substantial light on the nature of corporate governance in Kuwait, its development over time, and its effect on firm performance.

Ownership structure in this sense relates to the mix of large and small, individual, and institutional, local, and foreign, and private and public sector shareholders, among others. The expectation is that certain ownership structures are able to improve firm performance, however measured, through sound management and the well-considered allocation of firm resources. Some types of ownership arguably improve professional conduct and monitoring in business and accordingly limit the opportunities for risk, fraud, or embezzlement. Others widen the network of business contacts. Still others bring with them business expertise to be used within the firm. All encompass corporate governance, leading to the first research question in this thesis:

RQ1: How does ownership structure affect Kuwaiti firm performance?
The second research question examines the association between boards of directors’ characteristics and firm performance. Boards of directors are largely responsible for firm performance, ensuring the development and implementation of strategies and policy that enable the firm to perform for the benefit of shareholders, usually implemented on a day-to-day basis through delegation to management, which the board also monitors and supports on an ongoing basis. However, boards are also responsible for a firm’s compliance with its legal, regulatory, and industry obligations through ensuring the organisation develops and implements appropriate systems, processes, and procedures for this purpose. Only by examining board characteristics in detail and over time can knowledge be gained about which of their many features work most effectively. Thus, the second research question for this thesis is:

**RQ2**: How do board of directors’ characteristics affect Kuwaiti firm performance?

Clearly, boards of directors will have the most effect on overall firm performance, with desirable features of boards, board members, and board meetings in this regard being their dedication to the task, their expertise and knowledge, and their independence and freedom from conflicts of interest (Bhagat & Bolton, 2019). However, audit committees also have a role to play, such as enabling the board to appropriately perform its overall compliance role and ensuring that it not only meets its mandated obligations to external parties, but is also able to manage the risks to the firm from its activities. Audit committees also provide an internal service in monitoring and supervising the firm and an external service in assisting investors in making confident and informed decisions (Burke, Hoitash, & Hoitash, 2019). In much the same way as boards, audit committees, along with the quality of their audits, are a function of their understanding of the business and assessment of the risks to the firm, the expertise of the audit committee members, and their effectiveness and engagement. Accordingly, this motivated the third research question:

**RQ3**: How do audit committee characteristics affect Kuwaiti firm performance?

In contrast to the three previous research questions, which are largely quantitative in nature, the fourth and final research question explores several immeasurable variables that have the potential to affect the relationship between corporate governance and firm performance in specific contexts. Obviously, the legal setting is one significant factor, as corporate governance lies at the interface of finance and law. However, cultural factors, including religion, tribal systems, and political circumstances, could also explain the
relationship between corporate governance and firm performance, especially in a country like Kuwait, leading to the fourth research question:

**RQ4:** What role—if any—do cultural, social, political, and economic circumstances play in moderating the relationship between corporate governance and Kuwaiti firm performance?

Corporate governance essentially pertains to the practices, rules, and guidelines that oversee the management–shareholder relationship in a firm, in addition to firm’s stakeholders. It adds value in terms of growth and financial stability through reinforcing market confidence, economic efficiency, and the integrity of the financial market. Therefore, corporate governance is regarded as distributing rights and responsibilities among different individuals and parties in a firm, whether this be the board of directors, stakeholders, shareholders, or management. Moreover, it also seeks to ensure clarity and understanding surrounding corporate affairs and the rules and procedures surrounding them. Corporate governance has recently become an important issue in understanding firm decision-making and its relation to firm performance, with many studies considering the impact of various factors on good corporate governance processes and practices, including culture, the level of development, and legal and political circumstances. These are all important, given the fundamental need for firms to attract investment capital, enhance corporate performance, and reduce investor risk.

Finally, the research questions directly led to evaluating firms’ financial and operational systems. In addition, immeasurable variables such as cultural factors, religion, and political and tribal systems directly affect the relationship between firm performance and corporate governance.

### 1.6 Research Gaps and Contributions

This study has been established to cover numerous gaps in prior studies and to present new results related to these gaps overall—particularly in the context of Kuwait. Several gaps and contributions are listed to achieve the main aim of this study:

- The literature review shows that most prior studies examining the association between corporate governance mechanisms and firm performance tend to limit the measures to one or more characteristics of corporate governance and involve them in firm performance. Accordingly, this research reviews similar studies in a much wider context and includes a greater variety of research techniques.
• Several different reasons have been outlined as underpinning the selection of Kuwait as a case study in this research. These are: first, the majority of other works completed in this arena are known to use developed countries, which therefore highlights the need to investigate whether or not developing countries would demonstrate the same findings; second, thus far no study has been carried out in this field in the context of Kuwait; third, the results garnered through this work could help the country’s researchers to circumvent the issues in future studies related to this one.

• Corporate governance in Kuwaiti firms is still in the development and growth stage compared to other developed and developing countries. Prior studies covering corporate governance in Kuwait are few and limited, whereas this study considers a starting point of a large number of future studies investigating the impact of corporate governance on different fields.

• This study addresses a gap in the literature relating to corporate governance in the social, political, and economic environments in Kuwait as a specific case among GCC countries.

• There are several immeasurable issues that could affect the nature of the relationship between corporate governance and firm performance in industrial and services firms in Kuwait, such as culture, religion, education, skills, social structure, the political system, and economic circumstances.

• This empirical research adds to prior studies on corporate governance and firm performance and will centre on providing an in-depth investigation of the factors affecting countries, drawing on the framework of the institutional perspective in a developing country.

In conclusion, the contributions provide further justification for the thesis. Also, this thesis encourages understanding of and insight into the most fundamental factors recognised as influencing the link between firm performance and corporate governance. Moreover, the study considers that countries adhere to their own legal and cultural practices, as well as their social environment. Accordingly, this thesis is geared towards the situation and systems applicable to Kuwait. As a result, the work facilitates investors in the country, as well as government officials, market regulators, and accounting professionals, in devising new investment and strategic policies. Considering that Kuwait has come to recognise and partake in much discussion surrounding this issue, with the
government implementing its first Capital Markets Authority on September 7, 2010, investment in corporate governance is seen to be growing in importance. This is apparent when considering that debates has been ongoing in relation to the difference made by corporate governance and whether it adds value. As a developing region, empirical works concerned with the value of corporate governance and company performance are few in Kuwait. Finally, the findings make a contribution to the body of research examining corporate governance on an international scale in various economic and social arenas.

1.7 Thesis Outline

This thesis comprises eight chapters.

Chapter 1 has provided the background for the study and the motivation behind undertaking this work and outlines the research questions answered within this thesis. Chapter 2 provides an overview of corporate governance in Kuwait, including the history, society, and economy of Kuwait and an overview of the KSE. This chapter also reviews the regulations and corporate financial reporting market, sheds useful light on corporate governance mechanisms in Kuwait over the course of the last decade, and compares the corporate governance codes within the GCC.

Chapter 3 presents a detailed discussion of the underpinning theory of corporate governance including agency, stakeholder, and institutional theory and firm performance. The chapter also presents the conceptual framework used for empirical models used in the remaining chapters.

Chapter 4 compares the review of corporate governance mechanisms, discussing the empirical and theoretical literature relating to corporate governance mechanisms and firm performance. This chapter also defines corporate governance and reviews the literature related to the global corporate governance mechanism (i.e., boards of directors’ characteristics, audit committee characteristics, and ownership structure). Finally, this chapter critically discusses the relationship between corporate governance mechanism and firm performance (i.e., ROA, ROE, and TQ).

Chapter 5 examines ownership structure, corporate governance reform, and firm performance, as well as the association between ownership structure and firm performance in Kuwait (Paper 1). The chapter provides a current theoretical and empirical assessment of the literature concerning corporate governance reform and firm performance in Kuwait, shedding light on the gaps and limitations in the existing
literature. This chapter also briefly describes the methods used to measure ownership structure and firm performance proxies—including descriptive statistics, correlations, variance inflation factors (VIF), heteroscedasticity, OLS regression, and robust regression.

Chapter 6 (Paper 2) outlines the connection between institutional reform, organisational change, and firm performance to investigate the relationship between boards of directors’ characteristics, audit committee characteristics, and firm performance proxies (ROA, ROE, and TQ). The chapter provides a current theoretical and empirical assessment of the literature concerning corporate governance characteristics and firm performance, in addition to the process of developing the research hypotheses while considering the prior literature. This section discusses the gaps, contributions, and limitations included in this research, and also briefly describes the methods used to measure the boards of directors’ characteristics, audit committee characteristics, and firm performance proxies—including descriptive statistics, correlations, and robust regression.

Chapter 7 (Paper 3) presents a semi-structured interviews analysis—titled “Qualitative insights into the relations between corporate governance reform, management decision-making, and accounting performance: Semi-Structured interview evidence”—in order to answer the research questions relating to immeasurable variables. Accordingly, this chapter reveals several immeasurable issues that could impact the nature of the relationship between corporate governance and firm performance within Kuwaiti industrial and services firms (e.g., culture, religion, education, skills, social structure, the political system, and economic circumstances). Finally, it fills a gap that did not exist within the prior literature in line with social and political issues, examining the development of corporate governance in the social, political, and economic environments within Kuwait as a specific case among GCC countries.

Chapter 8 concludes the thesis by providing a summary of the research methodology, gaps, contribution, significance, and limitations, as well as the key findings and results, as derived from each research paper. Finally, this chapter provides several useful recommendations and indicates valuable guidelines for future research in the area.
Chapter 2: An Overview of Corporate Governance in Kuwait

2.1 Introduction

This chapter directs attention towards the overall history of Kuwait, with emphasis placed on its economy and the development of the Kuwait Stock Exchange (KSE). Furthermore, the corporate governance laws and regulations applicable in the country, such as any key aspects that have some degree of influence on the research findings, are reviewed.

This chapter comprises the following sections: Section 2.2 discusses Kuwait in terms of its background, while Section 2.3 provides a generalised view of the country’s economy. Section 2.4 then discusses the stock exchange in Kuwait, while Section 2.5 provides insight into the market divisions of Kuwait. Following this, Section 2.6 directs attention towards corporate financial reporting and regulation, while Section 2.7 discusses the Kuwaiti business environment in terms of shareholder rights, boards of directors, and disclosure and auditing. Next, in Section 2.8 is considered the value and importance of corporate governance in Kuwait, which is recognised as one of the key aspects potentially influencing performance. Section 2.9 presents a comparative summary of the corporate governance codes in the Gulf Cooperation Council (GCC). Finally, Section 2.10 provides the chapter summary.

2.2 Background of Kuwait

Kuwait is officially known as the State of Kuwait. The country is located in Western Asia and is an Arab region. The Arabian Peninsula surrounds the country on the north-eastern boundary and may be found at the peak of the Arabian Gulf. The country has borders with Saudi Arabia to the south and Iraq to the north, as shown in Figure 2.1. Casey (2007) stated that the country name Kuwait is derived from the word kut, meaning ‘small fort’.

The country’s history dates to the 18th century, when families and tribal groups migrated from the central Arabian Peninsula to the north-east arena. Among these populations, the Al-Sabah family was one of the most well known; they belonged to the
Al-Anazi tribe. This provides an explanation as to why Sabah is regarded as the first of Kuwait's monarchs, as Sabah was elected by his peers and started the country's first royal family. Throughout the period spanning 1756–1762, Sabah ruled; however, from 1899 through to 1961, the country entered into an agreement with the British Empire, which stated that the UK would manage the security and protection of the country. Furthermore, the UK also stated that it would not play any role in the domestic issues of the country. The agreement was terminated on February 26, 1961, which became known as Kuwait’s Day of Independence.

The Al-Sabah family has ruled the country since its founding, that is, from 1756 until the present day. The country spans an estimated 18,700 square kilometres, equal to around 7,000 square miles. The Public Authority for Civil Information (PACI, 2018) stated that the country's population stands at approximately 4.5 million people; just under one-third (30.35%) are Kuwaiti citizens, while the remainder are labourers or immigrants from other countries. Arabic is the official language, followed by English, which is taught in education and widely used in business. The official currency is the Kuwaiti dinar (KD), and when compared to the Australian dollar, the exchange rate is believed to be in the region of KD1 to AUD4.72 (Central Bank of Kuwait [CBK], 2019).

![Map of Kuwait](image)

**Figure 2.1. Map of Kuwait.**

Kuwaiti City serves as the political and economic capital of the country. The country is generally viewed as being very liberal in the Arab region. Importantly, it is recognised as having the world's fifth-greatest reserves of oil and petroleum. At present, this source is responsible for 90% of the government's income and 10% of non-oil revenue. It is
recognised as the eighth-wealthiest country in the world when considering per capita income. The World Bank defines it as a high-income economy (CBK, 2017).

2.3 Kuwait’s Economy: An Overview

Kuwait’s economy is recognised as one of the most fundamental across the Middle East because it is one of the greatest oil exporters across the globe. Several critical elements have influenced its important and valuable economy, at both international and regional levels. The key industries in the country are building materials, cement, foodstuffs, oil, petrochemicals, sea water desalination, and ship building and repairing.

The year 1946 marked the onset of a noteworthy period in Kuwait’s economy; this is when the first oil shipment was made. However, the benefits of oil were first reaped in 1934, when an oil organisation known as the Kuwait Oil Company was founded. Following this, from a commercial perspective, was the discovery of oil in 1938. In the 1960s, the Kuwait National Petroleum Company was established by the Kuwaiti Government as a joint venture. However, by 1978, the government had achieved control of the petroleum sector. Subsequently, the Kuwait Petroleum Corporation (KPC) was established, which brought together all industrial sectors within one holding company. Accordingly, there was a greater degree of effectiveness in the control of those sectors.

At present, the KPC is charged with the management of eight large organisations, each of which has its own area of specialisation in regard to transportation, manufacturing, and oil production (KPC, 2018).

Most of the economy in the country is dominated by the public sector, with natural gas, oil products, and oil sector revenues garnered from crude oil responsible for approximately 65.7% of the country’s overall gross domestic product (GDP); an estimated 95% represents exports of goods and services, while the same figure is attributable to government revenue. In Kuwait, crude oil reserves are approximately 104 billion barrels, representing 8% of all oil reserves in the world (International Monetary Fund [IMF], 2019).

Kuwait’s economy has experienced several reforms implemented by the country’s government, and has achieved increases in GDP in prior years, with consistent progress despite numerous economic crises, such as the Al-Manakh crisis in 1982, the Iraqi occupation in 1990, and finally, the global financial crisis in September 2008. Kuwait’s economy demonstrated significant rates of growth as a result of ever-increasing oil
prices throughout the years 2003–2008, along with inflation rates reaching 10.6% in 2008. The Central Bank of Kuwait (CBK) has taken several actions to counteract inflationary pressures as it ended the pegging of the Kuwaiti dinar (KD) to the US dollar in 2007 and accordingly pegged the Kuwaiti dinar to a weighted basket of currencies of the countries recognised as having the most fundamental commercial and financial links with Kuwait. Furthermore, the Kuwaiti Government implemented several precautionary measures aimed towards consolidating conditions in the local financial and banking arena, geared at maintaining stability in this field (IMF, 2011). As outlined in the CBK’s (2017) annual report, GDP increased to KD 39,769 million throughout 2017 in comparison to KD 38,667.1 million for 2012.

Table 2.1. Kuwait’s GDP and Oil Prices

<table>
<thead>
<tr>
<th>Year</th>
<th>GDP (billions of dollars)</th>
<th>Average oil price ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1978</td>
<td>16</td>
<td>14.95</td>
</tr>
<tr>
<td>1982</td>
<td>22</td>
<td>31.83</td>
</tr>
<tr>
<td>1986</td>
<td>18</td>
<td>14.44</td>
</tr>
<tr>
<td>1990</td>
<td>18</td>
<td>23.19</td>
</tr>
<tr>
<td>1994</td>
<td>25</td>
<td>15.66</td>
</tr>
<tr>
<td>1998</td>
<td>26</td>
<td>11.91</td>
</tr>
<tr>
<td>2002</td>
<td>38</td>
<td>22.81</td>
</tr>
<tr>
<td>2006</td>
<td>102</td>
<td>58.3</td>
</tr>
<tr>
<td>2010</td>
<td>115</td>
<td>71.21</td>
</tr>
<tr>
<td>2014</td>
<td>164</td>
<td>85.6</td>
</tr>
<tr>
<td>2018</td>
<td>120</td>
<td>58.15</td>
</tr>
</tbody>
</table>

Source: InflationData.com and WorldBank.org

Kuwait’s GDP, as well as its oil prices, increased ten times throughout the period 1978–1982. Moreover, GDP was USD$16 billion, while the oil price per barrel was, on average, $14.95; this increased to GDP of USD$22 billion dollars and an average oil price of $31.83. As a direct result of the Iraq–Kuwait invasion in 1990, the price of oil decline dramatically to $23.19, causing the GDP to fall to USD$18 billion. Until 2014, increases were witnessed across GDP and oil price domains. More specifically, GDP achieved USD$164 billion while the average price of oil reached USD$85.60. In 2018 the average oil price dropped to USD$58.15. This drop was not surprising under the circumstances of the Middle East revolution. In 2017, the Central Bank of Kuwait
reported that the oil industry provides as much as 89.2% of the government’s revenue budget and more than half (52.7%) of all GDP. Oil demand and prices ultimately depend on the economic and political situations across the world, which provides some rationalisation for the Kuwaiti Government and the National Assembly seeking to have their income source decentralised (see Table 2.1).

2.4 Kuwait Stock Exchange (KSE)

The Kuwaiti Government recognised the need for joint stock organisations and shareholding firms following the discovery of oil. Such entities were required to ensure the country’s infrastructure development. Organisations were therefore encouraged to issue shares on the KSE, which was established in 1952. The first public organisation to trade on that particular market was the National Bank of Kuwait, and the KSE was created in an effort to provide a reliable mechanism geared towards large investment project trading. It has been successful in achieving balanced development across both public and private sectors. Accordingly, good levels of wealth have been derived from satisfying investors’ desires. Organisations in the country have become very self-disciplined in raising KSE finances. To achieve this, firms need to be well managed and direct their attention towards performing in line with expectations (KSE, 2001).

Employment of the country’s citizens has been emphasised by the Kuwaiti Government since 1960. Focus has been placed on improving levels of domestic liquidity so that people can achieve greater savings and investments. As a result of the significant demands made in regard to public shareholding companies and the significant number of Kuwaiti investors, the Kuwaiti Government has directed investment towards the KSE, which has subsequently encouraged the birth of and rise in a number of unqualified investors and unofficial brokers. Accordingly, in 1960, the first Company Law No. 15 was established by the government with the aim of ensuring new firms would undergo regulation. This law was then followed by Commercial Law No. 27, which was enacted in 1962. As emphasised by this law, Kuwaiti firms may be established abroad; however, the need to regulate the KSE became prominent in the late 1960s.

The KSE is recognised as one of the oldest financial markets in the country, as well as one of the biggest in the Gulf region when considering capital value. Its operations were first initiated following its independence from Britain in 1962, and share trading was
first witnessed in 1952. Importantly, a spiral in stock prices and volume in the over-the-counter market was induced by speculative trading; however, in 1976, the market collapsed. As a result, the government restricted the listing of new firms on the exchange by implementing trade and margin regulations. The KSE was established and stabilised by 1977 (Al-Yaqout, 2006). Furthermore, in 1979, Souk Al-Manakh (a parallel stock exchange) was established as a direct result of the government’s restriction on the establishment of public entities. The market in the country was highly unregulated, and several Gulf-based organisations traded that were not in line with the requirements outlined for official market listing.

As such, in 1981, forward trading bans became more relaxed, resulting in a dramatic increase in official and parallel market prices. The government subsequently decided to implement several reforms with the objective of improving the stock market’s overall efficacy. Hassan et al. (2003) outlined the underlying reforms. Several key measures are recognised as effective in achieving improved efficiency and functioning across the KSE: the written auction system and the limit system on price alteration, both of which align stock transactions. Official and parallel markets were separated, with emphasis on disclosure rules in an effort to maintain and ensure market transparency pertaining to the markets and the need for brokerage organisations and dealers to register. Finally, disclosure rules were implemented with the aim of ensuring market accountability and transparency (Hassan et al., 2003).

Following the events of the Al-Manakh crisis, the Kuwaiti Government showed a disregard for Gulf organisations, with the Al-Manakh market not governed by law. The government believed that every individual was liable for their own investment-related choices; therefore, it was not able to predict that trading on this particular market would increase so much, which ultimately caused the issue. In the earlier months of 1982, the Al-Manakh market and KSE trading exceeded expectations; various investors from other countries were also encouraged to invest in the country, and many illegal brokers and large investors exploited the opportunity to speculate on share price. Owing to the lack of requirements to publish financial data and analyses, investors were unable to gather information pertaining to share prices (Al-Yaqout, 2006).

Following the Al-Manakh market crisis, the government directed its focus to regulating the KSE. In August 1983, the KSE was positioned as an independent financial institution, and administration fell to an executive committee. Significant growth has
been demonstrated by the KSE in recent years, with the market now representing one of the largest stock exchanges across the Middle East (Al-Hares, AbuGhazaleh, & Haddad, 2012; Bouresli & Aldeehani, 2017). In 1984, a new trading system was implemented by the KSE, which provides widespread derivatives and stocks for investors. One hundred and eighty different organisations were included across eight different industries. It is independently run to achieve market efficacy growth. The Kuwait Clearing Company was founded by the KSE as a settlement house for all trades carried out on the KSE, with the objective of circumventing the risk of broker default, as well as ensuring share prices and monitoring speculation movements. Finally, in an effort to control the market’s dealings and activities, a committee was established to set rules to organise market business.

The KSE and the Kuwaiti economy are also impacted by a number of other factors. For example, various corporate scandals have occurred across the world, such as the credit crunch and the Dubai crisis, both of which had notable effects on the economy and markets. Kuwait’s revenue resources are directly affected by oil prices: oil increase causes an increase in domestic liquidity, thus causing capital flow into the country. When this happens, the government invests in projects that have been held back because of budget deficits, which results in notable increases in the share price index. When there is a decline in interest rates, there is an increase in loans and in stock prices (Al-Saidi, 2013). Moreover, in February 2010, a Capital Markets Authority Law, focused on determining the CMA, was passed by the Parliament. Subsequently, the KSE was supervised by the CMA, and public and private subscriptions were also supervised by this entity. The CMA also has the role of regulating and supervising acquisitions and mergers, and this grants the CMA further broad regulatory and supervisory authority over investment companies. In addition, the CMA is charged with overseeing investment companies’ activities with regards to the KSE (Al Mutairi et al., 2012).

2.5 Market Divisions

The KSE is broken down into primary and secondary markets, which are official and parallel, respectively. The regular market is recognised as the equity market, where sell and buy orders are matched in line with price-time priority (5% of the firm’s capital). The ‘small cap’ market is referred to as the parallel market and includes organisations that have less capital or less than three years’ continuation. Across the KSE, and based
on the sample of study, the KSE had two periods: Period 1 from 2010 to 2011, which included eight sectors (non-Kuwaiti, investment, insurance, real estate, industry, service, food, and banking) and Period 2 from 2012 to 2017, which included thirteen sectors (oil and gas, basic materials, industrials, consumer goods, health care, consumer services, telecommunications, banking, insurance, real estate, financial services, technology, and parallel).

For the period spanning 2010–2017, total trading volume is shown in Table 2.2. As can be seen in Table 2.2, the sample had two periods: Period 1 was categorised based on the old KSE classification and Period 2 comprises thirteen sectors, with a fluctuation in total trading volume in the KSE during 2010–2017. When considering the oil and gas sector, share trading increased from 2.88% (2012) to 4.69% (2016). Moreover, share trading of basic materials and industrials was 0.46% and 11.11%, respectively, in 2012, then rose to 0.49% and 6.25%, respectively, in 2017. In 2012–2014, increasing from 0.01% to 0.30%, a lack of confidence in insurance shares trading was recognised among investors, causing trading at 0.01% in 2016. This also occurred in share trading in the technology sector: although share trading in this sector was 0.43% in 2012, the following year there was a negative trend, with figures at 0.40%, and 2017 showed 0.17%.

The services share trading flow demonstrated a steady, consistent performance, with share trading of the real estate sector at 27.97% in 2012 but at 32.58% in 2017. Moreover, a fall was recognised across the banking sector throughout this same period, with share trading at 6.71% in 2012 but at 13.14% in 2017. Furthermore, across the KSE’s financial services sector, 2012 showed the largest volume of trading sectors at 44.14%, with the end of the period showing 36.33% in 2017.

2.6 Financial System and Regulation in Kuwait

The Kuwaiti Government assesses and rationalises organisations’ financial reporting to ensure investors’ interests, and the interests of other financial report users, are safeguarded. The Ministry of Commerce and Industry and the KSE together issue most regulatory laws for listed organisations in the country. The most fundamental laws recognised in the country are Ministerial Resolution No. 18 (1990), the Stock Exchange Law (1983) and its amendments, and Company Law No. 15 (1960), which was issued by the Ministry of Commerce and Industry on October 19, 1960 (cancelled recently and
replaced by Law No. 25 of 2012) because the cancelled law was valid before the Al-Manakh crisis and until late 2012. Realistically, corporations under the new law are still defined in much the same way. Law No. 1 for 2016 regarding Companies Law states that organisations need to keep clear records at clearing agencies. In addition, the country issued the Executive Regulation for Law No. 7 for 2010, which relates to the establishment of the CMA and regulating securities. This regulation details that all joint stock organisations are required to deposit a record of stockholders upon the completion of the establishment process, with the deposit made at a clearing agency that has been afforded certification by the right authority.

As outlined in the Stock Exchange Law of 1983 and its amendments, to be listed on the KSE, organisations must adhere to various accounting stipulations. For example, organisations need to make audited annual reports available for the previous two years, with operating profit and a sound financial structure detailed and made available. The KSE has the authority to implement any additional requirements that do not need to be detailed on the KSE. Essentially, organisations need to present audited financial reports of profit and loss statements, as well as balance sheets, to the KSE.
Table 2.2. Total Trading Volume (Shares) 2010–2017

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-Kuwaiti</td>
<td>8% 5%</td>
<td>Oil &amp; gas 2.88% 3.38% 4.82% 4.43% 4.69% 2.84%</td>
<td></td>
</tr>
<tr>
<td>Investment</td>
<td>29% 28%</td>
<td>Basic materials 0.46% 0.23% 0.34% 0.22% 0.43% 0.49%</td>
<td></td>
</tr>
<tr>
<td>Insurance</td>
<td>0% 0%</td>
<td>Industrials 11.11% 12.24% 9.89% 9.77% 8.55% 6.25%</td>
<td></td>
</tr>
<tr>
<td>Real estate</td>
<td>24% 24%</td>
<td>Consumer goods 0.65% 1.06% 1.02% 0.74% 1.07% 0.99%</td>
<td></td>
</tr>
<tr>
<td>Industry</td>
<td>6% 6%</td>
<td>Health care 0.06% 0.04% 0.05% 0.07% 0.19% 0.01%</td>
<td></td>
</tr>
<tr>
<td>Services</td>
<td>25% 28%</td>
<td>Consumer services 0.57% 0.92% 1.14% 1.41% 3.00% 1.56%</td>
<td></td>
</tr>
<tr>
<td>Food</td>
<td>1% 1%</td>
<td>Telecommunications 4.47% 1.41% 2.28% 5.88% 5.72% 4.70%</td>
<td></td>
</tr>
<tr>
<td>Banking</td>
<td>7% 8%</td>
<td>Banking 6.71% 5.71% 8.27% 6.68% 12.39% 13.14%</td>
<td></td>
</tr>
<tr>
<td>-</td>
<td>-</td>
<td>Insurance 0.01% 0.23% 0.30% 0.06% 0.01% 0.14%</td>
<td></td>
</tr>
<tr>
<td>-</td>
<td>-</td>
<td>Real estate 27.97% 33.57% 24.83% 29.63% 26.20% 32.58%</td>
<td></td>
</tr>
<tr>
<td>-</td>
<td>-</td>
<td>Financial services 44.14% 38.58% 44.00% 36.93% 36.84% 36.33%</td>
<td></td>
</tr>
<tr>
<td>-</td>
<td>-</td>
<td>Technology 0.43% 0.40% 0.55% 0.37% 0.23% 0.17%</td>
<td></td>
</tr>
<tr>
<td>-</td>
<td>-</td>
<td>Parallel 0.52% 2.22% 2.51% 3.80% 0.61% 0.81%</td>
<td></td>
</tr>
<tr>
<td>Total (Million/KD)</td>
<td>12,526 6,059</td>
<td>- 7,216 11,389 6,176 4,010 2,880 5,728</td>
<td></td>
</tr>
</tbody>
</table>

Source: Kuwait Stock Exchange

The only professional body in the country, the Kuwait Accounting and Auditing Association, established in 1973, does not have any power to enforce the compliance of regulating professions. Recently, however, it has given advice to the government when this has been requested, although the function of the organisation remains limited to completing accounting standards courses and financial statement analysis.
2.7  Corporate Governance Mechanisms in Kuwait

Corporate governance has recently become a critical subject across the world, especially across emerging stock markets. Corporate governance has become recognised as fundamental in circumventing corporate management expropriation at the cost of minority shareholders. Although corporate governance is recognised as notably important in various countries, in Kuwait it lacks an approach for ensuring shareholder protection (Al-Wasmi, 2011). Several different schemes have aimed to deal with corporate governance in the country. As a preliminary step, the Chamber of Commerce and the Union of Investment Companies arranged a number of forums, conferences, and seminars focused on corporate governance with the aim of encouraging the government to devise and implement appropriate guidelines. The Kuwaiti CMA subsequently issued Law No. 7 and its amendments in 2010, and this was recognised as one of the objectives of the authority act, as detailed in Article 3 of this law. Essentially, this further reinforces the proper application of governance rules. More specifically, the Article details the following:

1. Securities activities should be regulated efficiently, transparently, and fairly.
2. Capital markets should be grown, and the investment instruments should be developed and diversified in line with the best international practice.
3. Investor protection should be improved and ensured.
4. Systemic risks stemming from securities activities should be minimised.
5. Requirements centred on complete and transparent disclosure should be obligatory to ensure fairness and transparency, and also to help reduce conflicts of interest and the use of insider information.
6. Compliance with and adherence to the rules and regulations in regards to securities activities should be enhanced and improved.
7. Public awareness pertaining to securities activities and the various advantages, risks, and obligations stemming from securities investments should be enhanced and developed.

In Kuwait, Resolution No. 25 of 2013 positions the issuance of corporate governance rules within the CMA’s control, placing value and importance on outlining and
implementing suitable, comprehensive corporate governance rules that highlight the need to ensure competitiveness, justice, and transparency across the market. Governance rules, therefore, centre on ensuring that shareholders are better protected through different principles, procedures, and systems. Moreover, good governance is centred on the promotion of three key activities: ethical behaviour geared towards ensuring dedication to good professional conduct and sound ethics; accountability and supervision; and administrating the organisation to ensure the very best distribution of power and responsibility, with distinct and separate functions. The Commercial Companies Law No. 1 (2016) is recognised as the most valuable resource in regards to listed companies and their governance structure. This particular law determines the requirements overseeing corporate governance, including the board of directors, auditing, disclosure, ownership structure, and shareholders’ rights, as discussed in the following subsections.

2.7.1 Boards of Directors

As outlined in Article 145, the board of directors is created as established by the organisation’s founding members, who hold a large portion of shares in the company. Members of the organisation are chosen in line with a shareholder vote at the general meeting, and the board’s overall responsibility centres on ensuring the firm’s compliance with association articles. Notably, the board’s structure is single-tier.

As noted in Articles 181 and 182 of the Company Law in Kuwait, all organisations are required to choose at least five directors who will hold their position for three years. This process is carried out through shareholder ballot-voting. The period for which the directors are chosen is renewable, and a listed company’s directors need to be qualified, without any inclination to commit breaches of honour or trust, and they must not have any link to or association with criminal or fraudulent activities. Furthermore, any individual director cannot be assigned the role of managing director or chairman if they hold such a position in another firm. Importantly, directors are unable to sell their share whenever they hold a position in the company. Without the approval of a general assembly, a director also cannot make any organisational secret or decision public, as stipulated in Article 194 and Article 195. Furthermore, in line with Article 188, any director (governmental, institutional, or individual) can assign a representative on his own behalf to the board. Moreover, as noted in Article 192, should any board director choose to resign his position, the position will then be taken by the largest shareholder.
Members of the board must meet four times every year. As communicated in Article 190, at least 50% of the directors, including three directors, must be present at each of the meetings. Through the board’s power, the company is managed in line with the law, general assembly resolutions, and articles of association. Moreover, the board’s power extends to the mortgaging or selling of company property, loans, the provision of guarantees for third parties, and the discharge of debtors from liabilities, which is restricted by the provisions of the articles of association (Article 184).

The company’s president is the chairman, who is afforded the right to sign on the company’s behalf, and this individual is also responsible for executing any resolutions made by the board. Should the chairman be absent, the deputy chairman is responsible, as detailed in Article 185. Notably, the board members and chairman assume joint liability for the company, third parties, and shareholders in regards to any fraudulent, misappropriation, or violating activities (Article 201 and Article 202). Furthermore, the board assigns most day-to-day operational functions to management; the only powers assumed and continued by the board include extraordinary decisions, which might include new investments, auditor selection, write-offs, and dividends.

Non-executive directors (NEDs) are also considered company directors; however, they are not involved in the everyday running of the company and the completion of activities in the way of executive directors. Importantly, NEDs are company board members and are therefore involved in board meetings. The law in Kuwait does not provide any detail regarding significant differences between executive and non-executive management; however, NEDs are usually appointed from high government officials who will provide the company with support when there are problems or when government permission may be needed. Accordingly, it is common for NEDs to be appointed from rich and influential families across Kuwaiti society. Notably, although some such individuals are appointed in line with their qualifications, personal links and connections are fundamental.

2.7.2 Shareholders’ Rights and General Meetings

Company shareholders are not involved in organisation operations; instead, they provide supervisory functions, including appointing and removing directors and auditors, attending general assemblies, gathering financial data, and approving annual financial statements. Laws in the country provide shareholders with support in
safeguarding their rights, enforcing rights, assisting in registration, and transferring ownership. As detailed in Article 178 and Article 179, all shareholders are afforded equal rights and liabilities in terms of receiving annual financial reports, disposing of shares, filling actions, receiving shares in property upon company liquidation, purchasing new shares, accessing company registers, participating in management and general meetings, and receiving dividends. Importantly, ordinary or common shareholders are also afforded the right to vote in general or extraordinary meetings.

The listing requirements of the KSE and in Kuwait’s Company Law state an obligation for all listed organisations to arrange a yearly general assembly. If the company does not adhere to this stipulation, the KSE will de-list it. Importantly, the board is required to prepare the meeting agenda, with the directors deciding the location and time of the assembly. The directors, government, and shareholders are afforded the right to arrange special meetings and organise a general assembly when there is an urgent situation. Moreover, notice of the meeting and the agenda must be published a minimum of 15 days prior to the meeting, with at least two Arabic daily newspapers detailing such events. The board of directors’ report should be made available to shareholders, along with the period’s financial statement and auditor’s report.

Shareholders can raise concerns at a general meeting. General assembly meetings are only considered valid when at least 50% of the members are present. If the quorum is not met at the initial meeting, then the board can request another meeting without conditions. Shareholders are given an attendance card, which allows them access to meetings and outlines the number of votes to which a shareholder is entitled (see Article 206). Votes may be made personally, or a proxy may be appointed to vote on their behalf (Article 208). The one-share-one-vote system is outlined and underscored by the law in the case of all firms in Kuwait, in addition to decisions resulting from a majority (Article 209). Should a poll be requested, the voting shares held by each individual present and voting on the issue determine the number of votes. Importantly, this enables a single individual who holds many shares to be afforded adequate weight in the decision-making process, in line with their investment in the company. At the general meeting, the chairman counts votes by a show of hands.

As noted in Article 211, the general assembly meeting might include any of the following:

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• A report of the activities and financial position of the company for the past financial year, as detailed by the board of directors.

• A report on the financial statement of the company provided by the auditor.

• A report on any violations recognised by the supervisory authorities in regard to any penalties the organisation has received.

• The company’s financial statements.

• The board of directors’ proposal in regard to profit distribution.

• The board of directors’ decision in regard to member discharges.

• The appointment and removal of members of the board of directors and the decisions made in regard to their remuneration.

• The appointment of the company auditor and decisions made in regard to their remuneration, or the board of directors’ authorisation in decisions made in regards to remuneration.

• The appointment of the Shari’a supervisory board for organisations operating in line with Islamic Shari’a law and hearing the report of such a board.

• A report detailing the transactions historically carried out or that will be carried out with related parties, and the identification of such parties in line with international accounting principles.

Shareholders’ financial liability may not be increased through general assembly meetings, nor do they mean that the percentage distribution from net profits will be reduced, as outlined in the articles of association, or that shareholders’ rights to institute legal proceedings against directors will be restricted (Article 180). In some instances, organisations might request extraordinary assembly meetings with the aim of discussing particular concerns, including making changes to the memorandum of the company of its association articles, or otherwise increasing or decreasing the capital of the organisation, disposing of the company’s overall undertaking, or merging with another firm (Article 218).

In the case of extraordinary meetings—which are commonly requested by board members or shareholders seen to hold at least 15% capital—directors may be removed
by shareholders before their period of office comes to an end. The board must come together to form an extraordinary meeting within 30 days of receiving such a request (Article 216). Importantly, an extraordinary meeting is only considered valid when attended by representatives making up three-quarters of the firm’s capital. Should this stipulation not be satisfied, the board is required to invite shareholders to another meeting, which must be attended by shareholders representing half of the firm’s capital (Article 217).

Dividends are one of the key concerns of shareholders. In line with the law, dividends need to be declared by shareholders in the general meeting; it is common for dividends to be equal to the amount recommended by the director of the firm. Importantly, organisations are required by law to pay dividends to shareholders from statutory reserves when profits have not achieved a particular level (Article 222).

2.7.3 Disclosure and Auditing

Disclosure is fundamental for all shareholders. In the specific context of Kuwait, disclosure spans two key sources, namely Companies Law and KSE regulations, both of which are applicable to all listed organisations. Disclosure information is detailed in the general meeting, including in regard to the company’s agenda, shareholder register, and remuneration pertaining to directors. All shareholders are afforded the right to receive the Official Gazette, which contains the balance sheet and a list of directors and auditors, in addition to information pertaining to profit and loss for the previous financial year (Article 221).

Company Law in Kuwait specifies that all organisations are required to assign an auditor at their general assembly meeting, where such an individual is required to complete an audit on the financial statements for the company’s upcoming financial year (Article 227). To ensure the auditor is entirely independent, an auditor is not permitted to be a servant or officer for the company. Moreover, auditors cannot be a partner of anyone employed by the company or otherwise employed for consultancy services (Article 228). Importantly, auditors are afforded the right to access all books and documents, and to complete an audit across all financial statements. Furthermore, shareholders are given information concerning the books and records analysed, and information concerning income statements and balance sheets (Article 229).
At the general assembly meeting, auditors are required to certify that they are satisfied with the reports and the information contained within, and that the profit and loss accounts and balance sheets are, to their knowledge, fair and true, and in line with the law. Auditors, therefore, adopt a key and fundamental role. Notably, the law does not stipulate that boards use an auditing committee to oversee external auditors. Auditors need to provide reports for all shareholders, where such reports might include the following (Article 230):

- Whether or not all information and explanations have been arrived at in order to ensure the sound completion of the audit.
- Whether or not the organisation has ensured all books of accounts have been properly maintained.
- Whether or not the profit and loss accounts and balance sheets are seen to be in line with the books of accounts.
- Whether or not the directors’ report is found to align with the books of accounts.
- Whether or not there have been any violations of the law or the company’s articles of association.
- Whether or not there has been any form of fraud or breach of contract between shareholders and the auditor(s).
- Any other data outlined as necessary by executive regulations.

As detailed in Article 199, any decisions made by the board and company should be communicated to shareholders. Board members are not permitted to enter a contract with the company unless shareholders provide explicit approval. Furthermore, the board needs to safeguard the interests of the shareholders. The KSE further ensures that organisations disclose all information considered necessary. Investors are afforded a greater wealth of information owing to regulatory requirements. Moreover, listed organisations are required to submit different types of information and statements, upon demand. As noted in Law No. 7 of 2010 in regard to the establishment of the CMA, organisations are required to provide the KSE with reports pertaining to those shareholders who hold more than a 5% share in the firm.
2.8 Essential Kuwaiti Corporate Governance Code Enhancement

Kuwait is largely acknowledged as being a desirable nation in terms of financing opportunities. Kuwait is also traditionally acknowledged as one of the most rapidly expanding nations post-1950s (triggered by the conclusion of the oil revolution). Furthermore, Kuwait was one of the few nations putting itself forward to other leading marketplaces post the 2008 stock market crash (i.e., Japan, the UK, the US) to evade any negative impacts associated with the financial crisis; thus, it increased the high quality of the market. As a result of this self-introduction, and with the ultimate objective of evading any potential issues spurred by the financial crisis, as well as expanding the markets within Kuwait, the country established two novel laws, namely, the Kuwait Companies Law and the CMA Law.

Introduced in 2010 (two years after the financial crisis), the Kuwaiti CMA did not meet the above Kuwaiti objectives. Bouresli and Aldeehani (2017) stated that it was largely incapable of adopting and expanding Kuwaiti firm performance—which was ultimately what it had been designed to do—because of the numerous limitations and inconsistencies in its policies and rules. As a result of this failure, the New Companies Law (comprising the related executive regulations and Law No. 1 of 2016) was established, with the key objective of tackling any present disadvantages or inconsistencies.

While Kuwaiti regulators began working to establish a corporate governance code (which would hopefully result additional firm transaction and structure organisation), Kuwait was transferred into a novel arena in 2013 in adherence to the corporate governance code (Al-Saidi & Al-Shammari, 2014), which resulted in elements of firm performance being enhanced. For example, discrepancies between managers and owners were reduced (agency theory) and transparency increased.

The voluntary corporate governance code concluded in 2015, and during this time most industrial services and organisations within Kuwait adhered to only some aspects of the code. Alfraih and Almutawa (2017) acknowledged that this was largely because such a code would resolve a few issues. Numerous elements (e.g., firm transparency, firm performance) of Kuwaiti firms were enhanced because of this code.
2.9 Corporate Governance Codes in Gulf Cooperation Council (GCC)

This section presents a comparative summary for corporate governance codes in the GCC (see Table 2.3).

Table 2.3. GCC (Gulf Cooperation Council) Codes of Corporate Governance

<table>
<thead>
<tr>
<th>Code of corporate governance</th>
<th>Kuwait</th>
<th>Saudi Arabia</th>
<th>United Arab Emirates</th>
<th>Bahrain</th>
<th>Oman</th>
<th>Qatar</th>
</tr>
</thead>
<tbody>
<tr>
<td>Code title</td>
<td>Kuwait Corporate Governance Code</td>
<td>The Kingdom of Saudi Arabia’s Corporate Governance Regulations</td>
<td>Corporate Governance Code of the United Arab Emirates</td>
<td>Corporate Governance Code of Bahrain</td>
<td>Corporate Governance Code</td>
<td>Corporate Governance Code of Qatar</td>
</tr>
<tr>
<td>Currency used</td>
<td>The Kuwaiti dinar</td>
<td>The Saudi riyal</td>
<td>The United Arab Emirates dirham</td>
<td>The Bahraini dinar</td>
<td>The Omani riyal</td>
<td>The Qatari riyal</td>
</tr>
<tr>
<td>Status</td>
<td>Voluntary</td>
<td>Voluntary</td>
<td>Voluntary</td>
<td>Voluntary</td>
<td>Voluntary</td>
<td>Voluntary</td>
</tr>
<tr>
<td>Regulator of finances</td>
<td>Capital Markets Authority</td>
<td>Capital Market Authority</td>
<td>Securities and Commodities Authority</td>
<td>Bahrein’s Central Bank</td>
<td>The Capital Market Authority</td>
<td>Financial Centre Regulatory Authority of Qatar</td>
</tr>
<tr>
<td>Attentions of the code</td>
<td>The guidelines comprise codes that outline the deliveries and prerequisites linked with the government rule adoption. Founded on the grounds of 11 guidelines detailing far-reaching ideas the establishment should implement.</td>
<td>The rules, principles, and directions provided are linked with the Saudi Stock Exchange.</td>
<td>Founded on three key modules: corporate governance, institutional discipline standards, and general provisions.</td>
<td>Founded on the grounds of nine key ideas founded on the grounds of global optimal implementations corporate governance.</td>
<td>The rules, functions, jobs, board’s professional conduct, groups, executives, directors, company secretary (etc.) are the topics of the 14 guidelines partitioned for the Code for Corporate Governance, which apply to all Muscat</td>
<td>Founded on the grounds of the 42 articles (derived from the seven modules) detailing control systems, adoption, disclosures, honesty, the rights of stakeholders, and a list of other services.</td>
</tr>
<tr>
<td>Code of corporate governance</td>
<td>Kuwait</td>
<td>Saudi Arabia</td>
<td>United Arab Emirates</td>
<td>Bahrain</td>
<td>Oman</td>
<td>Qatar</td>
</tr>
<tr>
<td>-----------------------------</td>
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<td>------</td>
<td>-------</td>
</tr>
<tr>
<td>Securities Market-listed establishments. This has additionally been founded on the grounds of the principles of accountability, honesty, sensibility, and impartiality.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Size of the board</th>
<th>Five or more members</th>
<th>Between three and eleven members</th>
<th>N/A</th>
<th>Between zero and 15 members</th>
<th>Between five and 12 members</th>
<th>N/A</th>
</tr>
</thead>
<tbody>
<tr>
<td>Director (non-executive)</td>
<td>Majority</td>
<td>Majority</td>
<td>Majority</td>
<td>Majority</td>
<td>All</td>
<td>Majority</td>
</tr>
<tr>
<td>Board of director (independent)</td>
<td>N/A</td>
<td>⅓ of all members OR two members (whichever is greater).</td>
<td>⅓ of all members.</td>
<td>Data unavailable.</td>
<td>⅓ of all members OR two members (whichever is greater).</td>
<td>⅓ of all members.</td>
</tr>
<tr>
<td>Yearly board meetings</td>
<td>Six</td>
<td>Four</td>
<td>Four</td>
<td>Four</td>
<td>Four</td>
<td>Six</td>
</tr>
<tr>
<td>Size of the audit committee</td>
<td>Three</td>
<td>Between three and five</td>
<td>Three</td>
<td>Three</td>
<td>Three</td>
<td>Three</td>
</tr>
<tr>
<td>Members of the audit committee</td>
<td>One or more members</td>
<td>One or more members</td>
<td>Majority</td>
<td>Majority</td>
<td>Majority</td>
<td>Majority</td>
</tr>
<tr>
<td>Annual audit committee meeting</td>
<td>Four</td>
<td>Four</td>
<td>Four</td>
<td>Data unavailable</td>
<td>Four</td>
<td>Six</td>
</tr>
<tr>
<td>Size of the remuneration committee</td>
<td>Three</td>
<td>Between three and five</td>
<td>Three</td>
<td>Three</td>
<td>Three</td>
<td>Three</td>
</tr>
<tr>
<td>Independent members of the remuneration committee</td>
<td>One or more</td>
<td>One or more</td>
<td>Two or more</td>
<td>Majority</td>
<td>Data unavailable</td>
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</table>
### Code of Corporate Governance

#### Annual Remuneration Committee Meeting

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<tr>
<td>Annual remuneration committee meeting</td>
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#### Duality of the CEO

- A committee member should not be elected as board chairman. The CEO should not be elected as the board chairman.
- Upon completion of one year of service, there will be a CEO appointment as board chairman. The board chairman cannot have held an executive position. The chairman of the Remuneration Committee, the Audit Committee, or the Risk Committee should not be elected as board chairman.
- No committee members should be elected as board chairman.
- Data unavailable
- Members of other committees should not be elected for board chairman. Board and Audit Committee chairman places are available. The subsidiary’s and parent’s CEO should not be matching.
- Remuneration Committee and Audit Committee members should not be elected as the board chairman, nor should any member chairing more than one committee. No executive position should be undertaken by the board chairman. The Audit Committee should not have the same chairman as that of any other committee.

#### Allowing for Disclosure

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<th>Code of Corporate Governance</th>
<th>Kuwait</th>
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<tr>
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#### Rights of the Shareholder

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<tr>
<td>Rights of the shareholder</td>
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<td>Yes</td>
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Note: All of the data presented above has been founded on the grounds of the relevant country’s GCC (Corporate Governance Code).
2.10 Chapter Summary

This review into Kuwait’s market has established that various regulations and laws oversee the market, in addition to various corporate governance mechanisms. Several key factors should be highlighted:

- Kuwait’s capital market does not offer high liquidity and is dominated by a small number of organisations; similarly, trading volume is not significant. Little improvement has been seen across the equity market. Trading is thin and stock prices are noisy. Moreover, organisations are not inclined to maintain high disclosure.

- The practice of sound corporate governance has not been well developed or implemented in Kuwait, predominantly owing to a lack of dispersed ownership. For example, organisations in the country have few outside directors, equity-based incentives for management, high takeover attempts, and an absence of proxy fights.

- The board is not required by Company Law to maintain an audit committee with the task of observing external auditors’ functions.

- Any organisation’s founding members must have a high degree of control in regards to the business world and be able to influence management decisions through imposing their representative on the board or management. The board of any company tends to have many different family members and owners.

- The board members, CEO, and chairman are not well organised. In general, the role of the CEO is also held by the chairman.

Several challenges first need to be overcome to gear the CMA towards applying and adhering to the rules of corporate governance. For example, one challenge is the social relations pertaining to concentration of ownership across companies and their causes, such as privatisation, family businesses, and companies that are established through government initiative. Another is the complications regarding powers between companies and the CMA, the Ministry of Trade and Industry, and the Central Bank of Kuwait. Lastly, there are also obstacles to corporate governance in regard to the appointment of independent members and shareholder culture.
The following chapter discusses the theoretical perspective and conceptual framework related to corporate governance and firm performance within prior studies, providing a strong overview of theories related to the overall research objectives (e.g. agency theory, stewardship theory, stakeholder theory, resource-dependency theory, institutional theory, and transaction cost theory).
Chapter 3: Corporate Governance Theory

3.1 Introduction

It was concluded in the previous section, this chapter literature review, that a minuscule amount of focus has been directed to Kuwait within research concerning the correlation between firm performance and corporate governance. Furthermore, we can conclude from the earlier section that elements such as agency theory, stewardship theory, stakeholder theory, resource-dependency theory, institutional theory, transaction cost theory, and corporate governance inner workings have been the subject of very few such studies concerning the roles they play in influencing the relationship between firm performance and corporate governance in firms in Kuwait. With this in mind, this section will explore this topic in terms of its linked schools of thought and investigations so as to form a complete conceptual framework on the topic—and, in an attempt to garner the ways in which firm performance in Kuwaiti organisations is impacted by the various corporate governance elements, this investigation additionally aims to construct a comprehensive corporate governance framework, wholly rooted in the Kuwaiti context.

Guaranteeing that conflicts of interest are eliminated, stakeholder interests are borne in mind, honesty and culpability are maintained, and a high total value is provided to stakeholders, corporate governance principles are, according to Tanjung (2020), of high importance. This can be seen from its high rates of implementation, and the general view that it is positively influential within this context.

Decision-making authority, the extent of responsibility used in accordance with strategic decisions, power allotment, and appropriate resource placement are some of the varying business elements that the system focuses on (Puni & Anlesinya, 2020; Thorne, Ferrell, & Ferrell, 2011). Indeed, to guarantee interorganisational high performance, corporate governance places high importance on complete control and culpability being held at the strategic level. It is worth noting that, according to Yermack (1996) and Beiner et al. (2004), corporate governance and firm performance are possessing a positive relationship in previous studies. Furthermore, development can be seen when the firm’s resources are used proficiently—as is promoted by corporate governance (OECD, 2004).
According to Al-Najjar and Clark (2017), when it comes to credit (which allows for low-rate financing prospects), corporate standards are raised with the implementation of effective corporate governance; indeed, when firms use competent governance, they are likely to garner cheap capital because of the enhanced cash flow that such governance facilitates. According to Kavitha, Nandagopal, and Uma (2019), general economic proficiency and monetary immovability on both a national and an international scale can be attained through corporate governance, and, at an organisational level, those who implement effective corporate governance are better able to allocate their resources more appropriately and to utilise the appropriate control mechanisms. This further reinforces affluence and development within such an organisation.

This chapter is structured as follows: Section 3.2 presents the theoretical perspective on corporate governance and firm performance. Section 3.3 outlines the theoretical framework of the research. Section 3.4 discusses the development of a conceptual framework for this study. Finally, Section 3.5 provides the chapter summary.

3.2 Corporate Governance and Firm Performance: A Theoretical Perspective

According to Cuomo, Mallin, and Zattoni (2016), Durisin and Puzone (2009), and Turnbull (1997), economics, law, accounting, and finance are just some of the areas from which the theories underpinning corporate governance have been obtained. It is these theories that this section will endeavour to deliberate, while bearing in mind our theme of the relationship between firms’ financial performance and their employed corporate governance. Agency theory, stewardship theory, stakeholder theory, resource-dependency theory, institutional theory, and transaction cost theory are perhaps the most well-known theories concerning corporate governance and are thus the most commonly investigated within the literature. A comprehensive explanation of many of these theories is outlined by Clarke (2004).

As stated by Filatotchev and Boyd (2009), the vast majority of the research conducted within this area has been done on the grounds of agency theory—which may be unsurprising, considering that the financial aspect of corporate governance is typically tackled through a quantitative research method—and that is exactly the aim for the current study. Nicholson and Kiel (2007) and Haniffa and Hudaib (2006) do point out that much of the current literature has considered agency theory as well as information asymmetry, political financial implications, resource-dependency theory, manager signalling, and
stewardship, among others. According to Filatotchev and Boyd (2009) and Van, Gabrielsson, and Huse (2009), this also results from the need to use multiple theories within recent studies on corporate governance—a notion that might seem to contradict the ordinary understanding that agency theory typically forms the basis of any research within this area.

We can see from the earlier literature, including studies by Tanjung (2020) and Claessens and Yurtoglu (2013), that there are a multitude of current debates concerning corporate governance and firm performance, and which theoretical viewpoints are most appropriate when examining them. This is a particularly hot topic, considering that corporate governance is largely acknowledged to form the foundation of contemporary firm operation and management. Particularly when it comes to the theoretical viewpoints on corporate governance operations, which strive to find a compound understanding of a given topic (Lawal, 2012), there is an additional issue: one overall definition of corporate governance has not been reached, largely because each sector feels it comprises several. The works of Claessens and Yurtoglu (2013), Harrison and Coombs (2012), and Letza, Sun, and Kirkbride (2004), centring on stakeholder theory, agency theory, and corporate governance, a range of critical theories in the field, list the likes of stewardship theory, resource-dependency theory, transaction cost theory, agency theory, stakeholder theory, and institutional theory as being essential to corporate governance (Abdullah & Valentine, 2009). Hence, as our topic of discussion in the next section, a total of six theories will be employed within this study so as to sufficiently examine the KSE’s relationship between firm performance and corporate governance.

### 3.2.1 Agency Theory

According to Donaldson and Davis (1991) and Berle and Means (1991), agency theory acknowledges that corporate governance is essential when it comes to guaranteeing that principal–agent risks are avoided and that any other issues are navigated. Indeed, agency theory has either borne or influenced a great many studies on corporate governance, and it examines the operations and relationships between employees working to fulfil the goals of principles/stakeholders. It also analyses how and why conflicts of interest may come about. Notably, an ‘agent’ in this context can be defined as a person who bears the burden of another’s workload on their behalf. According to Donaldson and Davis (1991), agency theory implies that all individuals within a given organisation are dedicated to navigating and fulfilling their own interests. Similarly, Daily, Dalton, and Cannella
(2003) point out that workers are often dissatisfied at the prospect of forfeiting their own interests so as to align their interests with those of others. With this in mind, we can view corporate governance as an organisation’s means of governing and reducing any inter-staff conflict (Berle & Means, 1991), as well as as a theory with self-interest at its foundation.

Lessening taxes as a means of making investment appear more appealing would be an example of one of the critical aims of corporate governance: to urge managers to make decisions by what will appear most attractive to stakeholders (Shleifer & Vishny, 1997). Indeed, according to Fama and Jensen (1983a), good corporate governance has been witnessed to tackle conflicts of interest more proficiently between managers and stakeholders, in turn lessening the agency problem. Such conflicts of interest are a frequently encountered cause for agency costs, as found by Jensen and Meckling (1976)—which surely indicates that more focus should be directed towards such conflicts of interest between minority and majority stakeholders of organisations in which said stakeholders own 50% or more of the total equity. Further, another source of agency cost is taxes on dividends (Berzins, Bøhren, & Stacescu, 2019). Finally, while tax shock has been found to lead organisations to having reduced financial demands because it increases the cost of paying dividends (Bradshaw, Liao, & Ma, 2019), the leading shareholder is required to trade the positive against the negative impact of increased shareholder conflicts.

As can be seen from the fact that the current literature states that solid explanations underpin the notion that corporate governance has a substantial impact on the influence of host countries in appealing to international investors, issues with corporate governance within developing countries centre on their standing in the market, as well as their potential to develop. This, of course, also has a direct impact on the wealth of such nations. According to Naeem and Li (2019) and Rueda (2000), however, all is not lost: strong corporate governance and corresponding policies are likely to appeal to investors.

According to Hart (1995), Sappington (1991), and Jensen and Meckling (1976), the relationship between large organisations is as follows: managers/agents are employed by owners/principals. The owners/principals recompense the agents (typically in pecuniary form) for governing the organisation in accordance with their interests. As can be easily perceived here, such large organisations tend to implement a framework which, at its very core, exercises a boundary and hierarchy between agents and principals. As has been
explored by Fama and Jensen (1983b) and Jensen and Meckling (1976), agency theory can be utilised to investigate the possibly challenging dynamic between agents and principals. Such a challenging dynamic comes about as a result of conflicts of interest between the two parties.

The key assumptions underpinning agency theory are contracts not being free when it comes to applying and writing (Fama & Jensen, 1983a), the individuals in question having restricted or limited rationality, managers being able to exploit their own interests instead of stakeholders’ (Demsetz, 1983; Jensen & Meckling, 1976), and agents and principals receiving data via asymmetrical distribution. Hence, the theory indicates that principals are not in a position to accurately calculate the leading managers of the organisation because of the asymmetrical data allocation between stakeholders and managers.

According to Jensen and Meckling (1976), the incurred agency costs include bonding costs (non-/financial costs of building structures or systems to guarantee that managers are acting upon stakeholders’ interests), residual losses (the result of self-interest-spurred actions that do not align with shareholder interests, and also thought by Fama and Jensen [1983a] to be the total value of the profit lost when the costs of a contract outweigh its advantages), and monitoring costs (the result of stakeholders’ governing of manager actions).

According to Sappington (1991), higher rewards are often reported as needing to be given to risk-averse agents as encouragement to exert themselves; although a given agent’s efforts are not entirely perceptible and, therefore, easy for the principal to measure, the performance or result within agency theory relies on the agent’s labours, as well as the risks that present themselves in the process. Indeed, according to Hart (1995), Sappington (1991), and Jensen and Meckling (1976), agency theory takes the stance that managers and stakeholders share a relationship that resembles a traditional principal–agent one; that is, owners hire managers to manage and run the organisation in the owners’ best interests, and the managers are paid to compensate them for their efforts. Considering this glaring issue within agency theory, it is clear that an equilibrium between risk-taking and proficiency needs to be outlined (Hart, 1995)—perhaps by principal implementing other monitoring processes to minimise the costs attributed to information symmetry, as the agent’s taking of their own desired actions may then be reduced (Arnold & De Lange, 2004; Sappington, 1991).
In order to oversee and calculate the efforts being made and, in turn, reward such work appropriately, the principal requires data because they may not already be wholly aware of such information. Otherwise, the principal’s needed efforts are unlikely to be met by managers, and this underwork would be left under the radar (Jensen & Meckling, 1976). According to the likes of Jensen (1993), Dhumale (1998), Jensen and Murphy (1990), and Shleifer and Vishny (1986), some of the many origins of such issues are free cash flow, the under- or over-investment decisions made by managers, and the earning of retentions and avoiding the difference seen by the positive value net and negative value net.. Indeed, according to Hart (1995), the incentive – risk-sharing puzzle is the original of the agency problem; practically speaking, the agents and the principals often have different motivations, and the agent’s motivations are supposed to be forming appealing rewards for efforts and safe risk-sharing.

The fact that the principal–agent paradigm delivers both conflict-solving (governance mechanisms) and conflict-evasion (corresponding incentives), and that it advises upon resolutions to the various problems encountered within agency theory, showcases that this paradigm possesses striking elements. Indeed, as is associated with property rights (since, when it comes to examining principal–agent relationships, the impacts of dispersing such property rights are crucial), agency theory centres on organisational arrangements, such as organisational/ownership structures. This conclusion is reached considering Fama and Jensen’s (1983b) definition of the part played by the board of directors when it comes to overseeing executive managers’ opportunities within big organisations.

According to Fama and Jensen (1983b) and Fama (1980), NEDs (non-executive directors) can provide significant organisational value, considering that they possess a monitoring mechanism as well as outside skillsets and knowledge. Indeed, because of the postulation that they are wholly independent and self-interested, agency theory postulates that when it comes to managing executives in the context of board of directors’ corporate governance, NEDs are critical (Fama & Jensen, 1983b). Further, while the lens of stewardship theory surmises that internal directors are better positioned to oversee management because they have knowledge of organisational mechanisms (Baysinger & Hoskisson, 1990), a positive causal link between the presence of NEDs (board independence) and firm performance is forecast by both resource-dependency theory and agency theory; the former ascribes heightened firm performance to the presence of NEDs
as a result of their influence over decision-making practices. In contrast, stewardship theory predicts that NEDs reduce firm performance; according to Bozec (2005), it maintains that NEDs’ monitoring functions are often hindered by their part-time position, which greatly impacts their role in the decision-making process.

According to Eisenberg, Sundgren, and Wells (1998), a given board’s aptitude in overseeing management is reduced as the board’s size increases, because this means a corresponding increase in communication and coordination issues. This, of course, only serves to worsen the current agency problem. Indeed, according to Jensen (1993) and Lipton and Lorsch (1992), as is mirrored in the fairly dissatisfactory performance of bigger boards, when NEDs play a key role in increasing board size, as discussed above, this means subpar communication and decision-making between members—although it also leads to a larger scope of skillsets within the board. According to Jensen (1993), merging the roles of CEO and chairperson can exacerbate current agency issues by thinning the CEO’s monitoring success; hence, in light of the fact that the chairman’s key concerns include managing the board and rewarding the CEO, agency theory advises totally splitting the CEO and chairman roles. Stewardship theory, however, advises that the CEO and chairman roles remain combined, on the grounds of the notion of ‘unity of command’, since it is believed that successful management can be attained in this way. According to Donaldson and Davis (1991) and Dalton and Kesner (1987), the reasoning is that increased knowledge and comprehension can be attained within organisational functions when this role is limited to just one person, which in turn leads to a drop in agency problems and, thus, a rise in firm performance.

In contrast, Jensen (1993) and Jensen and Meckling (1976) state that agency issues are reduced with managerial ownership contributing to the growth of agent enticements, as these are critical for making the interests of the principals and the agents correspond. This, in turn, reduces the taking of opportunistic actions. Indeed, as supported by Shleifer and Vishny (1997), controlling and large stakeholders possess the ability and incentive to oversee managers, so they greatly add to agency problem-solving. While agency theory will be implemented as the key theory underpinning this current examination, both stewardship theory and resource-dependency theory will be factored into consideration in instances where there are are relevant hypotheses, since neither of these theories by itself possesses a testable hypothesis that is associated with the ownership structure.
To summarise, rational managers will have to be provoked to carry out their roles of increasing shareholder value (and, in turn, drastically enhancing firm performance) through stakeholders possessing internal corporate governance mechanisms as a means of overseeing managers in order to lessen conflicts of interests between the principal and agent, because agency theory overall indicates that the current distinction between control and ownership within contemporary organisations means that agents are unlikely to fulfil the best interests of the principals. With the aid of corporate governance mechanisms that effectively recompense good behaviour and pinpoint any problems, these structural elements need to be complemented by practised attempts to control and oversee managers. Notably, agency costs (i.e., resulting financial implications of bonding agents, monitoring agents, and residual loss) can help to enhance firm performance and to lessen the agency problem, assuming such costs guarantee that managers still continue to act in the best interests of the stakeholders.

3.2.2 Stewardship Theory

Stewardship theory originated from the disciplines of sociology and psychology and indicates that executive managers are inherently reliable; thus, it stands in stark contrast to agency theory (since stewardship theory largely centres on managerial opportunistic individualism). It can be defined as follows: ‘A steward protects and maximises stakeholders’ wealth through firm performance, because by so doing, the steward’s utility functions are maximised’ (Davis, Schoorman, & Donaldson, 1997). According to Donaldson and Davis (1991), the theory stipulates that managers are incentivised to attain high firm performance; they want to be recognised by their peers as proficient in the field, since managers are inherently driven by the ultimate realisation of their organisation’s potential. The theory additionally assumes that managers take on the role of stewards, and that their motivations and behaviours correspond with those of the firm in which they are situated.

As stipulated by Davis et al. (1997), any given organisation needs to be created in a way that facilitates a given leader possessing the roles of both chairperson and CEO; the aim is that such a merged role will result in robust and collaborative control, ultimately leading to high performance and, hence, increased appeal to stakeholders (Donaldson & Davis, 1991). The notion of leadership, as well as whether (and how) the leader of a given firm is reliable (and whether their actions correspond with what will best benefit the firm), is the very basis of stewardship theory. Furthermore, stewardship theory notes that agency
costs can be dramatically reduced by handing discretion and power to the steward (Davis et al., 1997); they would have complete control over all the firm’s materials and resources and would be able to overrule with their authority in decision-making processes.

As noted by Donaldson and Davis (1991), stewardship theory also states that both executives and managers would be in a better position to ensure they make the most beneficial decisions for the firm by implementing stewardship theory, on the presumption that by doing so they would possess enhanced data and wisdom—especially when compared with that of external directors. The stewardship theory additionally forms the assumption that executives and managers are highly likely to better comprehend the business environment and workings than external directors because such individuals typically direct all of their attention in their careers to the firm they manage and direct. Furthermore, it has been noted that merging the roles of chairman and CEO would be beneficial because stewardship theory states that this facilitates managers and executives having access to additional power and authority within the workplace, so monetary performance within a given firm is likely to be improved when implementing the internal mechanisms and procedures of corporate governance (Clarke, 2004; Davis, et al., 1997; Donaldson & Davis, 1991; Pande & Ansari, 2014).

While agency theory expresses a preference for outside directors, stewardship theory takes a liking to specialist board members, the reasoning being that managers and executives are innately reliable, and so no conflicts of interest between parties should be expected. Saying this, it is worth noting that the firm’s organisational or environmental setting, or both, may influence the so-called ‘steward’; therefore, varying settings should be kept in mind when evaluating the variations that may arise in managers’ behaviour and the corporate governance practices implemented (Glinkowska & Kaczmarek, 2015; Turnbull, 1997).

3.2.3 Stakeholder Theory

Freeman (2010) was among the first individuals to put forward the notion of stakeholder theory as a part of the very basis of management, and over the past 30 years or so stakeholder theory has continued to be built upon and expanded. A stakeholder is defined as ‘… any group or individual who can is effected by the achievement of corporation’s purpose’ (Gomes, 2006), meaning the term can be attributed to any individual possessing any claim on the firm, whether directly or indirectly (Carroll & Buchholtz, 2014). Freeman, based on the notion that organisations should be held responsible to a wide
scope of stakeholders, additionally put forward a more general theory that could be implemented within organisations (Solomon & Solomon, 2004). Employees, consumers, nearby communities, stakeholders, suppliers, and the general public are some examples of stakeholders within a firm, and it is thought that only managers, consumers, nearby communities, the surrounding environment, investors, employees, business partners, and civil society should have any real influence over a given organisation (Wheeler & Sillanpaa, 1997). The policies and guidelines, whether formal or informal, that have been formulated within the relationship notably form the basis of the relationship between in-firm stakeholders (e.g., managers, owners, and employees) and the firm.

As stated by Freeman (1984), a stakeholder can be defined as anybody who possesses any impact and/or is impacted by the goings-on of a given organisation in the context of attaining the organisation’s goals. As can be seen here, corporate governance in the context of an organisation’s answerability to its wider community is often the subject of investigations into stakeholder theory corporate governance. Similarly to Freeman’s perspective, stakeholders are defined by the Organization for Economic Co-operation and Development (OECD, 1999) as the spokespersons of academia, the Indigenous community, non-governmental firms and stakeholders, consumers, wider communities, labour enterprises, churches, human rights groups, employees, suppliers or partners, and legislators. Achieving equilibrium in terms of the motivations and interests of these stakeholders could be the key to attaining any given organisation’s goals (Ansoff, 1965).

Stakeholder theory stipulates that all organisations should be handled in a way that is ultimately advantageous to every individual who possesses any form of stake within the organisation (i.e., partners, distributors, consumers, and employees), and is therefore often denoted as ‘the stakeholder model of corporate governance’. As an example, firm performance was found to be enhanced when organisations implemented the strategic stakeholder model (Berman et al., 1999), and, according to Christopher (2010), considering it is highly important in enhancing and employing useful governance, stakeholder theory seeks to construct positive relationships between stakeholders and organisations within a wider context. In a similar vein to this, we can debate that ‘… stakeholder involvement in corporate governance must rely on a culture of trust, community and consensus rather than of individualistic opportunism as in a shareholder-based system’ (Wright et al., 2003).
As was noted by Smallman (2004), the agency theory lens can be seen as a reduced version of stakeholder theory, since stakeholders’ incentives serve to increase the board of directors’ responsibility. Notably, the union of sustainable business systems’ stakeholder notion of corporate governance and corporate governance’s shareholder value–based view occurs as a result of the changeover that has occurred in corporate governance through the internalisation of capital markets (Feils, Rahman, & Sabac, 2018). As can be gathered from the above, communities related to environmental, ethical, and social matters are thought to be soon taken into account so as to increase the scope of stakeholders that are considered (Feils et al., 2018; Freeman, Wicks, & Parmar, 2004).

Considering that stakeholder gives agents the opportunity to direct their profit to other individuals rather than to stakeholders, stakeholder theory has faced many denunciations, including that exploitation could be encountered in the pursuit of attaining stakeholders’ desires in this way (Smallman, 2004). Such criticism aligns with the trend that most drawbacks of stakeholder theory are usually concerned with: how one can establish who can be classed as a trustworthy stakeholder. However, Deegan (2013) points out that, irrespective of whether improved monetary performance is attained through stakeholder management’s implementation, managers should focus on governing the firm at hand in a way that is primarily advantageous to stakeholders, since, morally, stakeholders should be treated justly by the firm.

Notably, very little debate and research has centred on stakeholder theory. The justification for this is often that potential investigators presume they are already aware of what ‘value’ means—that is, in the context of it being an economic value. Examples of this can be found in the work of Harrison and Wicks (2013) and Mitchell, Agle, and Wood (1997), where much discussion surrounds which individuals the managers direct most of their work towards, as well as who is reliable; essentially, who should be in such a position of power that they can access all of the firm’s resources. This stands in stark contrast to the theoretical ‘unity’ that stakeholder theory has proposed on paper, all the parties ultimately benefiting in the process; it has become clear that hostility is likely to arise among stakeholders when the values are only deemed to be economic, as this would naturally lead to a sort of competitiveness because the resources are then perceived to be limited (Freeman, Harrison, & Wicks, 2007).

According to Bosse, Phillips, and Harrison (2009), the vast majority of stakeholders have other interests, even though profit is still a critical element to a given organisation’s
central stakeholders. Indeed, most of the research conducted in this area is founded on the assumption that financial measures accurately encapsulate the value that arises as a result of the positive treatment of stakeholders—which, of course, fails to take into account the fact that this may not completely paint the full picture. Taking a step back to examine the full picture—or, rather, taking into account all the other variables that may come into play here—would allow researchers to gather a more well-rounded comprehension of the factors behind a given firm’s ultimate failure or success, data that would be invaluable for such firms and for future research.

As noted by Harrison and Wicks (2013) and Sachs and Ruhli (2011), managers typically direct their attention to the factors that appear to directly lead to increased firm performance, based on what calculations indicate, so from a manager’s viewpoint, a stakeholder’s viewpoint in terms of value is essential; this would help managers evaluate a wider scope of organisational values from the perspective of the relevant stakeholders. Indeed, as we can see from the above, lauded works within this field clearly indicate that additional assessment of the notion of a ‘value’ is needed, and this approach would provide managers with abundant data that would ultimately help them appeal to stakeholders through increasing the organisation’s perceived value in the stakeholder’s eyes.

It has been stipulated that communities and workers alike need to be considered and included within stakeholder relationships to increase monetary performance (Atkinson, Waterhouse, & Wells, 1997), and, similarly, Kaplan and Norton (1996) suggest that consumers should be taken into account when forming such relationships so as to improve upon the customer service front. Indeed, as noted by Freeman (1999), organisational managers who possess several relationship networks are particularly important players in the complete implementation of stakeholder theory.

Corporate governance primarily centres on how impactful various governance systems are in terms of increasing the commitment of different stakeholders and the long-term investment by such stakeholders (Maher & Andersson, 2000). As highlighted by Solomon (2010), the stakeholder method has become standard in the fields of finance and accounting, and so we can certainly say that stakeholder theory is now a strong character in several branches of corporate governance (Abu-Tapanjeh, 2009). Stakeholder theory is typically discussed in the context of its link to the wider population and the responsibility it casts on corporations in the relevant research, and evidently its inherent
mechanisms and the influencing characters involved in it can greatly impact the performance and ability of a given organisation (Bottenberg, Tuschke, & Flickinger, 2017). Indeed, as has been noted by Donaldson and Preston (1995), stakeholder theory has become a larger player in the bigger picture of corporate governance because it increases firm performance—a correlation that is found consistently in research within the field (Carroll & Buchholtz, 2014) and was supported by the research of Shahzad, Rutherford, and Sharfman (2016), who identified a positive link between increased shareholder value and effective shareholder management. In a similar vein, it can be argued that corporate managers should be required to bear in mind the potential impact all their decisions will have on stakeholders (Clarke, 2004). Similarly, it can be debated that a direct correlation between increased firm performance and the implementation of this approach could likely be identified by investigating the relationship between stakeholder performance and firm performance (Hillman, Keim, & Luce, 2001). Notably, since the board of directors bears all responsibility for the firm and its stakeholders, positive corporate governance must surely centre on stakeholders’ security that all actions are taken with their best interests in mind (Ljubojevic & Ljubojevic, 2011). This can be comfortably concluded because increased growth, profitability, and stability have been documented in the wake of stakeholder management (Pesqueux & Damak, 2005). An organisation simply cannot increase its value if management’s decisions do not act in the stakeholders’ best interests; we can say that because stakeholder theory ultimately endeavours to eliminate this prospect and drastically increase long-term value (Jensen, 2001).

In light of all of the above, we can conclude that the combination and implementation of stakeholder and agency theories serves to pinpoint the critical role organisations play when it comes to stakeholders. We can also surmise that when conflicts of interest do arise in the workplace, stakeholder-agency theory succeeds in pinpointing the factors that are causing such misalignment, as the stakeholder-agency merged theory ultimately centres on this area (Hill & Jones, 1992). Indeed, while stakeholder theory forms the basis of a given firm’s approach to maximising its value and facilitates the building of positive relationships between stakeholders, firms, and the wider social context, agency theory seeks to safeguard conflicts of interest within organisations via the appropriate monitoring offered by governance mechanisms. Hence, because it incorporates all the
factors that will ultimately succeed in enhancing firm performance, the utilisation of both theories would prove to be the most successful approach going forward.

3.2.4 Resource-Dependency Theory

Chiefly centring on organisations’ access to resources (e.g., profit, a variety of skillsets), resource-dependency theory centres on the material aspects of corporate governance. As defined by Pfeffer (1973), resource-dependency theory posits that it is critically important for units within corporate governance to have access to the materials they need when it comes to increasing firm performance. In this regard, NEDs are able to allow for retrieval of data, capital, and business and political connections (Htay & Salman, 2013; Kiel & Nicholson, 2003). The bigger scope of skillsets and connections they can provide access to leads to a dependency on NEDs when implementing this theory (Haniffa & Cooke, 2002; Haniffa & Hudaib, 2006). This, in turn, allows for reduced financial implications, as these materials are now easily accessible—another factor that serves to improve firm performance.

It could be argued that making a given board more eclectic would improve firm performance, since that would introduce a combination of materials and environments to the organisation (Pearce & Zahra, 1992). Pearce & Zahra (1992) also saw the conclusion that an organisation’s overall financial performance will be enhanced through the inclusion of external directors, since this will bring additional perspectives into play. Such a conclusion is backed by Carpenter and Westphal (2001), highlighting that connections help to keep business incentives stable in the face of international uncertainty; similarly, Bhatt and Bhattacharya (2015) suggest that diversity within a given board is necessary when it comes to fulfilling a firm’s needs and those of the future environment.

In order to enhance firm performance and provide additional value to the firm, according to Nicholson and Kiel (2007) and Muth and Donaldson (1998), resource-dependency theory utilises the board’s external links. Organisations do, of course, have to employ effective methods of accessing financial resources, and resource-dependency theory explains what organisations tend to do in this regard. It is probable that, in order to allow for such access to finance materials, a given organisation would employ a member of the creditor bank to the board if they were in a large amount of debt, since this is a simpler way of getting credit (Thompson & McEwen, 1958)—and, according to Mizruchi and Stearns (1988), when this is not the case, organisations are often urged to employ financial institution representatives to their boards. It has also been highlighted in the literature
that, when an organisation’s performance and/or stock prices are falling, it will often seek to employ financial directors (Kaplan & Minton, 1994). Furthermore, a notable relationship has been highlighted between the firm’s borrowing strategy and the financial representatives’ identities (Stearns & Mizruchi, 1993); Hermalin and Weisbach (1988) also advised that practised external directors should replace inside directors as firm performance declines. In a similar vein, a gap in accessed materials exists between developed markets and undeveloped markets because the latter face high costs, scarce capital, unstable economic development, and minimal progression of financial markets (Hitt et al., 2000). In light of this, it is clear that less-developed economies need to have access to external resources.

Expertise, materials, and other essential elements (i.e., consumers, social circles, partners, public policymakers, and legitimacy) are some of the critical things directors can bring to a given organisation (Hillman, Cannella, & Paetzold, 2000). These directors can be allocated to one of the following groups: business experts, who are old senior executives of large-scale, for-profit organisations to which they bring the above elements; community influencers (i.e., university staff, community organisation leaders, political leaders, and members of the clergy); insiders, who are current or prior firm executives offering skills in specified fields; and support specialists, who provide support in their specified respective fields (i.e., bankers, public relations experts, lawyers, and insurance firm representatives).

To summarise, we should be in a position to examine board composition and draw firm dependencies, since resource-dependency theory stipulates that directors are chosen in accordance with how easily they allow for access to resources. This, then, leaves us with the simple conclusion that resource-dependency theory indicates that a given firm’s board structure is indicative of its overall operational atmosphere (Boyd, 1995; Hillman et al., 2000; Pfeffer, 1972). From this, we can draw an example outlined by Hillman et al. (2000): an abundance of financers within a given board of directors indicates the organisation’s desire to garner capital cheaply—which is in itself indicative of the firm’s overall plan to make a big investment as a result of financial trouble. On the contrary, abundant access to resources could be indicated by the presence of a diverse range of employees within a firm.
3.2.5 Institutional Theory

As noted by Scott (1987), the key elements that make up institutional theory—that is, institutionalisation and institutional notions (Meyer & Rowan, 1977)—currently do not possess a unanimously agreed-upon definition because a multitude of angles can be looked at in this regard. A possible rationalisation for institutional theory becoming so commonly used in firm evaluation (Suddaby, 2010) is that put forward by Zucker (1987): it allows for a more detailed, well-rounded appraisal of firms; however, Suddaby (2010) and Zucker (1987) also outline two key problems with such a theory: the differentiation between resource-dependence rationalisations and institutional rationalisations because the authority in question is frequently transferred to governing the firm’s resource flow; and the need for a comparative method, since they are often invariant and international across firms. An example of an institutional setting mirroring the burdens stemming from external parties would be the justification of civil service reform. This change transformed the renovation of city governments to a more necessary element of contemporary, effectual governance structures.

According to Young et al. (2008), the rules and regulations of developed markets are potentially redundant within undeveloped markets as a result of divergent capital market constructions (Singh et al., 2005) and fragile firms (Gugler, Mueller, & Burcin, 2003). This is because they adapt to developed markets’ corporate governance methods, even though their institutional environments differ greatly from those of such markets. With this in mind, it is somewhat easy to understand why some may be wary of adopting agency theory. It can be debated that ownership structures and boards are not impacted by the institutional environment (Filatotchev, Jackson, & Nakajima, 2013; Mangena, Tauringana, & Chamisa, 2012). In a similar vein, we can comfortably conclude that, if we are to comprehend international corporate governance systems, it is absolutely essential that we acknowledge comparative examinations into institutions (Filatotchev et al., 2013). Finally, it has been highlighted that we must attempt to understand the prior literature concerning the ways in which corporate governance is influenced by institutions, and that the institutional divergences between developed and underdeveloped nations need to be both acknowledged and grouped (Acemoglu et al., 2003). Indeed, we can see that when it comes to encouraging the implementation of corporate governance within developing countries, some people are in a position to influence a wealth of institutional factors so as to garner individual desires and advantages—and, indeed, this
pinpoints the need to establish methods that both international and national organisations can utilise to encourage effective corporate governance practices within unstable environments, as well as the importance of investigating the impact of institutional environment on good corporate governance. With this in mind, a case study of Pakistan (a developing country) has been used within this current investigation, with the aims of investigating the core elements that facilitate good corporate governance, and then outlining the most effective methods for encouraging such corporate governance at an organisational level.

Scott (1995) defined recognised institutions as ‘… cognitive, normative, and regulative structures and activities that provide stability and meaning to social behaviour’; however, North (1990) outlined these as being manmade limitations that can outline the sort of communication that occurs between individuals. These two definitions can be considered together in line with Davis and North’s (1970) definition of institutional framework: ‘The set of fundamental political, social, and legal ground rules that establishes the basis for production, exchange, and distribution.’ We can say that when a given institutional framework has the ability to converse between organisations via suggestions of actions to take, any doubts or indecision can be made less overwhelming (Peng, 2002). Additionally, according to North (1990), day-to-day reservations can be lessened through organisations—especially when policies centre on controlling the actions taken.

As has been highlighted by North (1990), both formal limits (the economic covenant, political guidelines, and judicial verdicts) and informal limits (ideological norms and values [Scott, 1995], the public’s attitudes and behaviours) are integral to an organisation’s very framework. And it is informal limits that should act as substitutes upon the failure of formal limits, as this would guarantee consistency within firms (North, 1990). Similarly, according to Aguilera and Jackson (2003), the entire notion of ‘institutions’ should encompass organisation rules, cultural norms, and legal or regulatory bodies.

With the aim of enhancing any given institutional environment and to advance community corporate governance (Powell & DiMaggio, 1991), three models were created for collaborative use: corporate governance borrowing (the ‘imitative’ factor), the influence of professions on communities (the ‘normative’ factor), and government functions (the ‘coercive’ factor), which ultimately backs institutional theory.
As we can see by the respective impacts of the cultural and social system, the political system, and the law system on workers, managers, and owners (and the ways in which they conduct themselves within business), we can say that the institutional approach yields a notable impact on the corporate governance mechanisms of Indonesian banks (Umanto, Wijaya, & Atmoko, 2016). Similarly, an empirical study conducted in 2012 showcased the very strong link between organisations, culture, and corporate governance (Daniel, Cieslewicz, & Pourjalali, 2012), a finding that has ultimately resulted in an international exercising of a ‘gratefulness’ approach so as to alter organisational and cultural corporate governance mechanisms. Finally, it has been outlined that, when examining the influence of political economy, it is absolutely critical that the investigator acknowledges and bears in mind the subtle variances in the institutional approach and corporate governance (Grandori, 2004).

When it comes to answering this investigation’s key query—how institutional theory impacts the link between firm performance and corporate governance—it is appropriate to utilise institutional theory, since it offers practical solutions to such a query. According to Ayuso et al. (2016), considering they witness a wealth of unique and novel notions and philosophies from a range of contexts, organisations with high degrees of internalisation are given more opportunities for learning—something that has been seen to increase firm performance and facilitate organisations to influence their current resources on an international basis (Kaleka, 2012). The institutional theory is, notably, achieved via a method of exporting organisations, which leads them to adopt additional knowledge through being exposed to international markets (Martins & Yang, 2009; Vendrell et al., 2017). Furthermore, being present within such foreign markets can aid in building upon novel firm abilities, since in this way firms are exposed to foreign practices and challenges within their field.

As noted by Yang et al. (2020), institutional theory indicates that imitator performance has the potential to be directly affected by premature admission into the market, since those who were admitted late can have sway over their nonconformance to accepted industry practice (e.g., the market diversification strategy). Thus, we can conclude that the probability of a smaller industry imitating another’s norms increases as the number of organisations imitating early entries increases, since such an imitation has the potential to itself become institutionalised as more firms imitate early-entry firms.
Some firms have been formulated for the specific purpose of fulfilling this itinerary and others were already been established, so a wealth of organisations have participated in enhancing overall international firm performance, and in institutionalising good corporate governance practice. As noted by Li, Li, and Cai (2014), various local and global burdens are ultimately moulding international approaches to corporate governance; however, the current regulatory institutions were ultimately the ones who shouldered the burden of applying and creating the required policies. Notably, organisations and directors that do not act in accordance with such policies of corporate governance have begun facing injunctions and punishments, and in line with this, several leaders of nations have made it compulsory for organisations to act in accordance with such rules. From this, we can see the development of a society that, while being fairly relaxed in approach, is very firm on such regulations being instilled at a local level. It also important to note that a wealth of professional individuals and corporations are facing all three types of pressure (i.e., mimetic, coercive, and normative) from their neighbouring nations, even though such individuals and corporations are themselves normatively pressurising firms to implement good corporate governance. In a similar vein, an empirical study concluded that such positive corporate governance practices within Malaysia are strongly correlated to high firm performance in the nation at a micro level, and that corporate governance is only growing in this country as a result of being moulded by pressures to act in accordance with other nations’ practices (Khadaroo & Shaikh, 2007).

3.2.6 Transaction Cost Theory

It has been stated by Coase (1995) that firms can save money by focusing on the key elements of their business—and it is on Coase’s work, as well as this specific philosophy, that a wealth of transaction cost theory is based. Notably, information asymmetry, minimal negotiation, self-interested opportunism, asset specificity, and bounded rationality are, according to Learmount (2002), some of the in-contract problems that can be interpreted as being triggered by a range of wider issues regarding governance as a whole within a given firm. Furthermore, transaction cost theory operates on the premise that, when it comes to establishing where materials should be dealt, firms have replaced the market due to its scope. In light of the above, corporate governance could be defined as an organisation dedicated to aiding the firm in establishing any in-firm mechanisms and/or measures that can save any in-contract-issue-related costs.
In a normal scenario, any given firm can either outsource or carry out internal operations in order to attain their needed materials; however, transaction cost theory outlines the idea that, according to Williamson (1975), the high financial implications of executing contracts within the firm can lead to support for in-firm creation and markets as economic governance structures. According to Lamminmaki (2011), a quantitative evaluation in terms of the incurred advantages and disadvantages should be carried out to determine which method should be utilised—whether that be the one outlined above, hierarchy solutions (whereby managers direct and the hierarchy maintains the buying and distributing of resources), or market solutions (whereby individuals themselves purchase and supply such resources, and are only directed by fluctuating market prices).

Whether they materialise in the form of decision-making and negotiation finances (brought about by a need to buy something), information and search finances (brought about by the need to seek out a supplier), or enforcement and overseeing finances (brought about by the need to oversee output quality), transaction costs can come about when an organisation is handling their parties from both outside and inside the organisation. Since this minimises risk-taking and instability regarding pricing, enhances service and product quality, and evades transaction costs, firms should seek to internalise the majority of transactions made. The overall finances incurred as a result of providing services will be swayed by the way in which the firm is organised, as this ultimately impacts its aptitude for handling a large amount of transactions. Transaction costs can also be increased by opportunism—essentially when a figure acts in their own best interests—and by bounded rationality—allowing inexperienced and ill-informed individuals to make paramount business decisions. These factors are also particularly influential because they can massively influence a given firm’s ability to build upon and improve the services they provide. The uncertainty, frequency, and asset specificity specifically related to these factors largely determine this aptitude within the business at hand. Notably, any transaction costs submitted by business units on an in-firm basis are usually what trigger further transaction costs. Nevertheless, according to Luzzini et al. (2012), ignorance is the underpinning theme when it comes to studying transaction theory, no matter what study in the field is explored.

The managers’ and/or directors’ opportunism and bounded rationality, in the context of a given firm’s different layers, is essential when it comes to critically pinpointing and evaluating the incentive driving any given decision made within a business. Managers
behaving opportunistically is the opposite of appealing to prospective investors; therefore, establishing the extent of the opportunism at play can help form an accurate estimation of the amount of control and oversight needed by senior management to reduce transaction costs. Such opportunism can be measured by determining the extent to which the following factors are present: certainty, frequency, and asset specificity (the amount the manager is expected to receive) (Geyskens, Steenkamp, & Kumar, 2006). Indeed, as maintained by Tricker and Tricker (2015), firms should ensure they contrast internal controls and monitoring mechanisms that will reduce risk-taking by looking for markets that are simple to oversee, as this will reduce governance costs and the effects of bounded rationality.

To summarise all of the above, we can comprehensively investigate the meticulous and exact roles organisations play when it comes to the actions of stakeholders by using an integrated approach that comprises all of the discussed theories—theories that are ultimately compatible with one another because they tend to centre on a couple of the same elements. As an example of this, it has been concluded that the construction of institutional models similar to that constructed by Powell & DiMaggio (1991) has the potential to remedy any issues between stakeholders and managers (Hill & Jones, 1992).

Furthermore, while agency theory ultimately aims to attain equilibrium within the institutional structure by shielding smaller stakeholders from larger ones, and stakeholder theory aims to mirror rises in stakeholder wealth by highlighting corporate efficiency, stakeholder-agency theory centres on attaining equilibrium between stakeholder and manager interests (Filatotchev & Nakajima, 2010). We can thus conclude that merging all factors of corporate governance with the aim of furthering and enhancing firm performance will be the most advantageous method going forward.

### 3.3 Theoretical Framework

Donaldson and Davis’s (1989) stewardship theory, Pfeffer and Salancik’s (1978) resource-dependency theory, Coase’s (1995) and Hennart’s (2010) transaction cost theory, Jensen and Meckling’s (1976) agency theory, Freeman’s (1984) stakeholder theory, and Suchman’s (1995) institutional theory are the handful of theories that have been most commonly employed when investigating the topic of corporate governance, a notion that—despite being widely used on an international scale—has not, until recently, had any solid background to refer to (Abdullah & Valentine, 2009; Filatotchev &
Nakajima, 2010; Kota & Tomar, 2010; Larcker, Richardson & Tuna, 2005). There are abundant individual theories in this regard, so it seems clear that in order to obtain a clear representation of the extent to which firm performance is impacted by internal governance, an approach that combines the most relevant aspects of these theories (Eisenhardt, 1989; George, 2005; Kuhn, 2012) would be most effective.

This theory centres mainly on increasing value by lessening the agency problem so as to further appeal to stakeholders. Agency theory is the main theory employed in this investigation because it enables one to better explore the impact of corporate governance on a firm’s performance. Indeed, with the use of this theory, principals/stakeholders are much easier to examine, since the key characteristic of agency theory is the fact that it only concerns the principal and the agent. Ultimately offering researchers a workable hypothesis and a robust framework for investigating and drawing conclusions about the topic of conflicts of interest between agents and stakeholders by moderating such conflicts, leading to enhanced firm performance (Fama & Jensen, 1983a; Jensen & Meckling, 1976), the consensus of this theory is that differences in stakeholders’ and managers’ motivations result in the presence of conflicts of interest. As can be seen in the works of Jensen and Murphy (1990) and Dhumale (1998), such conflicts of interest can arise, for example, in situations where either under- or over-investments are made, where there are earning retentions, or where there is free cash flow, that do not correspond to the positive net present value rule.

A given organisation’s aptitude for increasing their shareholders’ income and, thus, enhancing firm performance, is often the result of good corporate governance operations overseeing the interests of both parties and constantly ensuring they correspond with one another—as is in line with agency theory. Indeed, according to Liu and Fong (2010), managing peoples’ abilities to create and apply suitable decisions is essential to high firm performance, as is ensuring that their interests correspond with those of stakeholders.

Notably, resource-dependency theory and stewardship theory do not offer any answers or frameworks to work off. Although these theories vary greatly from one another in terms of the way in which firm operations impact firm performance, they do share some of the same verdicts as agency theory. We can see in agency theory that stakeholders’ key objectives can be attained and conflicts of interest can be solved by ensuring both groups’ interests are compatible with one another; this is in light of Jensen and Meckling’s (1976) suggestion that creating incentives for managers is likely to urge agents to formulate a
total surplus. Indeed, agency theory works on the very basis that matching interests between both parties is essential; therefore, it is intuitive and somewhat necessary to provide such incentives for managers.

Institutional theory and stakeholder theory are both lauded by the OECD principles of corporate governance on the basis that stakeholders’ interests should all be kept in mind at all times by managers of organisations. Both of these theories indicate that firm performance could be enhanced via effective corporate governance strategies (Al-ahdal et al., 2020; Hennart, 2010). As seen in studies by Suddaby (2010) and Hennart (2010), both institutional and stakeholder theories are suitable for investigating the link between stakeholder management and corporate performance, as well as for studying any statements that have been issued regarding the notion of stakeholders as a whole. Both theories consistently leave us on the note that, based on the stakeholder management framework, enhanced firm performance is almost always directly linked to positive corporate governance.

On the grounds of the either positive or negative kind of corporate governance at hand, firm performance has the potential to be directly impacted by individuals starting to actively acknowledge that corporations are groups of individuals that are naturally diverse in their personal aims and outlooks (Abdullah & Valentine, 2009). Furthermore, according to transaction theory, the quality of a given organisation can be directly impacted by its very structure and how it is managed, since this theory postulates that such organisations have become so large in scale that they can effectively replace the market’s role of accessing and appointing materials.

Each basing their content on the conjecture that the performance of Kuwaiti services and industrial corporations is directly impacted by corporate governance operations, a conclusive conceptual framework and an acceptable answer for the study at hand can be garnered with the use of all of the theories (each showcased in Figure 3.1). While Figure 3.1 showcases abundant factors that can potentially alter the link between firm performance and corporate governance in Kuwaiti industrial and services firms, these theories were applied to this study’s framework as a way of establishing how stakeholder and manager interests can directly impact the quality of firm performance.
Figure 3.1. Theoretical Framework (Corporate Governance and Firm Performance).

3.4 A Conceptual Framework: Its Construction for This Study

Figure 3.1 illustrates the relationship between corporate governance, the factors affecting firm performance, and this investigation’s adopted theoretical framework, as this adequately mirrors the key objectives of this study: to evaluate each element of corporate governance and its relation to firm performance (return-on-equity [ROE], return-on-assets [ROA], and Tobin’s Q [TQ]), and to explore the overall relationship between firm performance within Kuwaiti industrial and services firms and their adopted corporate governance. The control variables here are the firm size, debt-to-equity ratio, leverage ratio, and cash from operating activities, while the dependent and independent variables are firm performance and corporate governance, respectively.
### 3.4.1 The Independent Variable: Corporate Governance Characteristics

A wealth of corporate governance characteristics were employed within this investigation with the aim of comprehensively exploring the link between firm performance and corporate governance operations—meaning they are naturally backed by agency theory, since they directly link back to the employed theoretical framework. The characteristics examined include: audit committee traits, such as number of meetings, expertise, size, and independence; board of directors’ traits, such as number of meetings, number of outside and independent individuals, and size; and the ownership structure and internal audit independence, such as government, family, and institutional ownership. These have all been discussed in the works of Al-ahdal et al. (2020), Kalelkar (2016), Adams and Jiang (2016), Hahn and Lasfer (2016), Khelil, Hussainey, and Noubbigh (2016), and Palmberg, (2015). This study has drawn the conclusion that these traits directly link to the applied framework, since a strong link between firm performance and corporate governance was noted in our findings. Notably, the key aim of the framework was to provide a concise, comprehensive understanding of the link between the performance and corporate governance mechanisms of Kuwaiti industrial and services firms.

### 3.4.2 The Dependent Variable: Firm Performance

While \( TQ \) has been widely implemented in studies within this field to calculate firm performance’s long-term proxy, other accounting financial ratios (e.g., ROE and ROA)—all for measuring short-term proxy—are less utilised in the literature. Therefore, all three were used as measuring tools to calculate the dependent variable of this study: firm performance.

As can be seen in the work of Heenetigala and Armstrong (2011), who noted a strong link between Sri Lankan corporate governance traits and an ROE, ROA, and \( TQ \) account of firm performance, a wealth of works in this field have garnered results that differ from the above. This can also be seen in the research of Haat, Rahman, and Mahenthiran (2008), who measured with ROE and ROA as proxies of firm performance and found that corporate governance had a notable influence over firm performance in Pakistan (2003–2005).
3.4.3 The Control Variables

In order to account for the other factors that could potentially influence the link between firm performance and control variables, we selected firm size, debt-to-equity ratio, leverage ratio, and cash flow from operating activities, which ended up being essential in establishing this relationship. The results from the literature concerning this relationship draw varying conclusions, as can be seen in the works of Jahanzeb et al. (2016), Durnev and Kim (2005), Nenova (2003), Himmelberg, Hubbard, and Palia (1999), and Agrawal and Knoeber (1996). We could say that firm size could serve to enhance performance, since an increase larger than the target will mean that the amount of resources available is larger (Jensen, 1986), and thus that smaller organisations are not in as good a position as larger ones are, since the latter can also formulate internal funds. Pointing out that larger organisations undergo difficult mechanisms so as to quickly fulfil firm goals, and that a larger firm would naturally require more advisors and decision-makers, Boone et al. (2007), Booth and Deli (1996), and Fama and Jensen (1983b) all maintain that a firm would naturally become more diverse in nature as it increased in size. Indeed, it was also concluded in a 2006 study that a larger firm size correlated with enhanced firm performance (Black, Love, & Rachinsky, 2006). This is also maintained by Serrasqueiro and Nunes (2008), who found that creating unique approaches and providing funds is easier for larger firms, and such elements have a direct, positive impact on firm performance.

This is not to say, however, that such a finding has not been called into question; indeed, it has been pointed out in a previous study that smaller firms are likely to adhere to corporate governance code requirements—if larger firms were to evade adhering to such requirements, it seems a given that these costs would only rise when this information was provided to the media, which would also lead to more examination by the media than for smaller firms (Garen, 1994). In line with this, Nenova (2003) maintains that smaller firms would be investigated far less, and be subjected to far less enquiry, than their larger counterparts, leading to financial implications for those in larger firms to extract private profits. In this vein, Agrawal and Knoeber (1996) concluded that, as a result of minimised control over in-firm operations and strategy-forming, smaller organisations will trump larger ones in terms of their efficiency. Hence, they noted an overall negative link between these two factors (firm performance and firm size). When it comes to tools for designing and guessing, an increase in firm size would surely mean that increased
management of such tools would be required, which would also mean more check-ins with principals and agents in terms of their interests and whether they still correspond (Jensen & Meckling, 1976). Additionally, Agrawal and Knoeber (1996) state that a firm’s costs would increase in line with the increase in firm size, since additional costs are needed to prevent employees from taking advantage of the new situation and acting in their own best interests, rather than those of the stakeholders. Notably, this investigation will calculate firm size in the same way as this field’s most significant studies (i.e., Al-Matari et al., 2012a; Elsayed, 2007; Lehn, Patro, & Zhao, 2009; Muth & Donaldson, 1998; Topak, 2011): by utilising the total assets’ natural logarithm.

In a similar vein, a wealth of the current literature has focused on the nature of the association between ownership concentration and debt-to-equity ratios. An example of this would be study conducted in 2019, which concluded that short debt equity and ownership concentration possessed a positive association. This conclusion is supported by agency theory and evidences the notion that the performance of conventional banks can be improved with managerial ownership and temporary debt ratio. Notably, these conclusions were drawn after the study of the behaviours shown between leverage and ownership structure (Fatima & Sohail, 2020). Furthermore, a similar study concluded that debt-to-equity ratios and firm size possess a positive relationship, while debt-to-equity ratio and institutional investors were found to possess a negative relationship (Hussainey & Aljifri, 2012). Fatima and Sohail’s (2020) study confirms that the association between firm performance and ownership structure is not impacted by leverage when it comes to instances of institutional ownership, and that the performance of Islamic banks is negatively impacted by institutional ownership and long-term debt ratio, since short debt equity possesses a negative relationship with ownership concentration. Such a notion is also supported by the findings of a 2015 study conducted in the same field (Alipour & Pejman, 2015).

Particularly in cases where the cash inflow is smaller than the cash outflow as a result of a disproportion, monetary troubles are handled by management, and, in line with this, when it comes to employees’ roles and fulfilling stakeholder interests, agency theory is directly linked to the governing of cash flow. According to Salehi, Lotfi, and Farhangdoust (2017) and Altman (2013), the governing of cash flow is absolutely paramount to the overall effective operation of a firm, since a cash flow error triggers an instant requirement for additional money and resources.
Notably, results from other studies indicate that an unstable state of cash flow actually does not wield much influence on other elements of the firm’s operation. An empirical study in 2013 investigated 80 of the Tehran Stock Exchange’s firms between the years of 2005 and 2011, and concluded that cash flow can accurately forecast any financial problems that could arise in the future (Namvar, Makrani, & Karami, 2013). Andreas (2017), however, completely dismissed cash flow as a trigger for monetary issues within a firm. Although we could conclude from Ball et al.’s (2016) study (which states that cash flow can forecast returns even a decade away) that similar economic factors are predicted to be shared between cash flow now and cash flow in 10 years, we could also take the stance that the current minimal cash flow will be better managed and slowly be amended within a 10-year period. Notably, Kordestani, Bakhtiari, and Biglari (2011) highlighted that there are divergences between firms possessing variable cash flow in terms of the monetary issues they have faced.

The firms we have selected reside in the developing countries of Libya, Algeria, and Sudan, which possess subpar corporate governance and policies. Therefore, we predict that the firms possessing subsidiaries will be more optimistic when it comes to earnings management, because a range of previous studies within the field (e.g., Dyreng, Hanlon, & Maydew, 2012; Guney, Karpuz, & Komba, 2020; Haat et al., 2008; Tang & Tikoo, 1999) have outlined that firms in developing countries and with subsidiaries are more likely than others to actively partake in earnings management. This level of engagement will be calculated with a dummy variable, whose value will be provided for each of the firms.

3.5 Chapter Summary

The theories undertaken within this investigation have been very commonly used in the prior literature within this field (i.e., one concerned with establishing the relationship between firm performance and corporate governance), and have been elaborated upon in detail in this chapter in regards to their applicability to this study’s goal: to establish the existence and nature of the relationship between firm performance and corporate governance. Theoretical perspective, firm performance, and corporate governance mechanisms are the three factors that comprise the framework used here, and this chapter has showcased the way in which we have constructed a suitable hypothesis to aid us in investigating the relationship between the performance and corporate governance of Kuwaiti firms.
Chapter 4: Corporate Governance Mechanisms

4.1 Introduction

Considering the fact that the assessment of results will be aided by obtaining a detailed comprehension of background corporate governance characteristics, this section will provide a summary of corporate governance mechanisms. The overall objective is to offer further understanding into a wealth of components (e.g., corporate governance characteristics [audit committee, board of directors, ownership structure], corporate governance definitions).

This chapter seeks to debate and evaluate the current existing published works focusing on firm performance and corporate governance of both developed and undeveloped nations—an appropriate sequel to the previous provision of insight into the corporate governance of Kuwaiti organisations and the Kuwaiti context as a whole. It has been previously showcased that by reducing organisational opportunities (specifically when it comes to building upon and expanding the financial position of organisations), both external and internal corporate governance mechanisms influence firm performance (Klapper & Love, 2004).

Wang, Yao, and Kang (2019) provide further evidence that organisations can be prevented from achieving their goals as a result of ongoing local rebellions—and, thus, that their quality can be reduced accordingly. When it comes to evaluating the quality of a given organisation, the majority of studies in the area centre entirely on firm performance; hence, they look to identify any factors that could alter firm performance (such as politics, recent Middle Eastern rebellions, and corporate governance).

According to Puni and Anlesinva (2020), Muravyev, Talavera, and Weir (2016), Adjaoud, Zeghal, and Andaleeb (2007), and Kiel and Nicholson (2003), ROE, return-on-interest, leverage ratio, ROA, return on capital employed, return on sales, and TQ are the main financial ratios often employed within the current literature as tools to measure firm performance.

According to Crowther (1996), the widely acknowledged so-called cornerstone of agency theory (i.e., the separating of managers’ [agency] and shareholders’ [principal] responsibilities) is one method of improving firm performance. In a similar vein, Puni and Anlesinva (2020) outline some of the approaches that have been implemented within the existing literature as tools to measure firm performance: the financial management method (i.e., concentrating on problems with cash flow and investment levels before evaluating the impact of funding sources
on firm performance), the sustainable growth method (i.e., merging the other methods), the capital structure method (i.e., concentrating on the elements affecting capital structure and, accordingly, firm performance), and the firm outcome resources method (i.e., acknowledging that firm outcomes are rooted in their sources). Furthermore, when it comes to organisations applying and enhancing risk-averse plans for the future, it has been established that firm performance is necessary for assessing the relevant business transactions (Maryska & Sladek, 2015).

This chapter opens with Section 4.2, which details the existing definitions of corporate governance; this section is followed by Section 4.3 and Section 4.4, which evaluate and debate the existing literature on firm performance and corporate governance, and outline a chapter summary, respectively.

4.2 Corporate Governance Definitions

According to Roche (2005), the task of finding a comprehensive definition for corporate governance is no easy feat because the field is unlimited. While the likes of Sundaram and Inkpen (2004) and Friedman (2007) stipulate that obtaining the largest possible shareholder wealth is at the forefront of any given firm’s tasks, Freeman (2010) maintains that firms are indebted to all shareholders, since they are all bound to influence firm performance in some way. Regardless of the opinions put forward by researchers in the field, it is undeniable that a wealth of variable elements means these definitions vary so much. One possible element, according to Armstrong and Sweeney (2002), is culture.

As can be seen from the fact that Public firms automatically obtain the central goal of ascertaining lasting value, which indicates that individual firms implement their corporate governance in diverse range—although it equally important to acknowledge that there are some similarities, too. Furthermore, while Rezaee (2009) stipulates that accountability for overseeing and managing an organisation (and ensuring both of these are carried out in line with shareholders’ interests) is the focus of value-protection, Maryska and Sladek (2015) maintain that value-creation focuses on shareholders, in terms of them applying and creating durable approaches that encourage long-term effective performance. Such viewpoints are sufficiently accounted for and conveyed in the following definitions.

The Organization for Economic Co-operation and Development (OECD) (1999) defines corporate governance as a structure in which firms are managed and guided in light of the OECD’s values. The methods by which performance is measured, firm goals are achieved, and
such goals are set are also established within this framework. Furthermore, tasks and entitlements are allocated here on a per-employee basis in light of the management, shareholders, board, and stakeholders. The OECD’s (2001) complete definition is as follows:

Corporate governance refers to the private and public institutions, including laws, regulations and accepted business practices, which together govern the relationship, in a market economy, between corporate managers and entrepreneurs (corporate insiders) on one hand, and those who invest resources in corporations on the other. (p. 13)

In another interpretation of corporate governance, the stakeholder approach and corporate governance could be seen as inherently affiliated, since corporate governance comprises a wide scope of consequences necessary for social equity, stability, the economy, and social wellness. Cadbury’s (2000) definition sums up this perspective fairly comprehensively:

Corporate governance is concerned with holding the balance between economic and social goals, and between individual and communal goals. The governance framework is there to encourage efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align nearly as possible the interest of individuals, corporations and society. The incentive to corporations is to achieve their corporate aims and to attract investment. The incentive for the state is to strengthen their economies and discourage fraud and mismanagement. (p. vi)

According to Clarke (2007, p. 83), complicated pursuits are harmonised in the name of value-creation because organisations want to attain social and environmental durability. Such a desire has often come about because of the importance being placed on stakeholder interests and/or shareholder returns—and this comes about because of the union between common international principles and a regional corporate governance system. With this in mind, corporate governance has previously been defined as a method whereby shareholders need managers to operate in accordance with their interests, since this will then allow for capital markets’ efficiency and reliability (Rezaee, 2009).

In a similar vein, corporate governance has been acknowledged by Kim and Rasiah (2010) as the connection between top management, the board, and shareholders within a given organisation—as well as their respective goals and focuses—that ultimately determines the organisation’s progress and performance as a whole. Based on this, three related theories are detailed next.
4.3 Corporate Governance Mechanisms and Firm Performance

As stated by Claessens, Djankov, and Lang (2000), legislators and academics generally acknowledge that all firms place a high priority on corporate governance as a part of their very framework. With the introduction of rapid technological advancements, financial markets, capital mobilisation, financial difficulty, liberalisation, and trade liberalisation, corporate governance has certainly risen in priority over the last 50 years or so—and, according to Fan, Lau, and Wu (2002), corporate governance mechanisms (processes utilised by firms as a way to rectify issues within corporate governance [Weimer & Pape, 1999]) can be divided into external mechanisms and internal mechanisms.

Kiel and Nicholson (2003) define internal governance mechanisms (e.g., audit committee, board of directors, and thus, board size, audit independence, board leadership, and board composition [Weir, Laing, & McKnight, 2002]) as the structural elements that alleviate the principal–agent issue. They also define external governance mechanisms as the elements that are external to the direct management or running of the organisation. Furthermore, according to Agrawal and Knoeber (1996), elements such as the board of directors and the audit committee qualify as internal governance mechanisms since they can only be used by decision-makers operating within the firm itself. Hence, as we can see here (and as indicated by Gillan, 2006), the primary goal of corporate governance mechanisms is to oversee the movements and processes of management. Accordingly, improving internal corporate governance mechanisms should surely enhance the overseeing of management and, thus, minimise any errors and help solve agency theory issues (Aldamen et al., 2012). Furthermore, as stated by Kyereboah and Biekpe (2006), the link and any interactions between firm performance and board characteristics could be organised by agency theory, because the likes of Lupu and Nichitean (2011), Kajola (2008), Hu and Izumida (2008), and Thomsen, Pedersen, and Kvist (2006) have confirmed that firm performance is, indeed, swayed by corporate governance mechanisms.

With the above in mind, the purpose of this section is to evaluate and debate the prior research conducted in both developed and undeveloped countries within this field; research within undeveloped countries regarding firm performance and corporate governance is particularly well-researched. In Asian countries, specifically, it has been noted that firm performance (and the attainment of organisations’ financial and social objectives) is particularly impacted—either positively or negatively—by the quality of corporate governance employed (Iqbal, Nawaz, & Ehsan, 2019). Furthermore, political issues, recent rebellions, corporate governance, and social issues are some of the things that have affected firm performance—especially in
Middle Eastern firms. Iqbal et al. (2019) also concluded that compliance with good governance operations will result in enhanced durability and income for organisations.

Saying this, organisations are unlikely to act in accordance with certain corporate governance unless there is clear, empirical data suggesting a direct link between such action and positive firm performance. Firm performance has been found to be positively related to foreign ownership, a large board of directors, and good corporate governance (Ciftci et al., 2019). This conclusion does appear to be valid, since factors such as audit size, corporate social responsibility, government ownership, and board size have similarly been documented as having a large amount of influence over the Gulf Cooperation Council’s (GCC) firm performance in Pillai and Malkawi’s (2018) investigation. In the same vein, the typical influences of corporate governance characteristics (e.g., audit committee size tends to lead to a reduction in firm performance) have been found to largely influence corporate governance (Moradi, Bagherpour, and Omidfar, 2017).

It has been previously showcased that by reducing organisational opportunities (specifically when it comes to building upon and expanding organisations’ financial positions), both external and internal corporate governance mechanisms influence firm performance (Klapper & Love, 2004).

As has been outlined by Muravyev et al. (2016), Adjaoud et al. (2007), and Kiel and Nicholson (2003), we can conclude from this section that in order to establish the impacts of varying factors on firm performance, a wealth of measuring tools (e.g., financial ratios, such as ROE, TQ, and ROA) need to be utilised.

4.3.1 Ownership Structure and Firm Performance

According to Florackis (2005), any organisation’s results are highly reliant on corporate governance, so it can be assumed that there is a dormant difference between managers’ interests and shareholders’ interests, and thus, that the relationship is always going to be tense due to the ever-present possibility of managers taking advantage of principals/shareholders.

The existence of an inherent conflict of interest between managers and shareholders is abundantly documented within prior studies in this field, and in line with this, agency theory outlines that managers are to act as shareholders’ (principles’) agents. And yet, as documented by Shleifer and Vishny (1997), Fama and Jensen (1983a), and Jensen and Meckling (1976), agents and managers often pursue their own interests, either using or reducing shareholder income in the process. Shareholders possess less drive to pursue their own interests because
the disadvantages of doing so would outweigh the advantages, so shareholders will probably not ensure that they closely oversee decisions made by managers (Grossman & Hart, 1986). Indeed, according to Jensen and Meckling (1976), agency theory offers an explanation for the agency-principal issue and the reduction of profits for shareholders it so often incurs.

It has been proposed that more concentrated ownership structures allow larger and more regulatory shareholders to aid in alleviating agency issues because they then possess the drive and ability to oversee managers (Shleifer & Vishny, 1986); this is largely because they then endure a shared benefit: control. It has also been stated that shareholders are better positioned to receive higher profit and share returns with the reduction of agency costs, because asymmetrical data is more likely to be avoided with the more active involvement of large shareholders—something that comes with the increase of ownership concentration (Demsetz & Lehn, 1985).

It could be supposed that conflict between shareholders and management could be avoided completely if both individuals were considered as one single body,—something that could be achieved with the implementation of managerial ownership (Jensen & Meckling, 1976); indeed, it has been maintained that agency-principal issues within agency theory arise as a result of large shareholders pursuing their own interests. We can see here that the interests of managers can be assumed to complement those of stakeholders in instances where managerial ownership is prominent. However, in cases where managers own a large stake, those managers have the potential to pursue their own interests over those of shareholders, which cannot be ignored.

Indeed, the topic of shareholder identity has been explored in a variety of the current literature in this field, with the likes of Douma, George, and Kabir (2006), Thomsen and Pedersen (2000), and Shleifer and Vishny (1997) outlining their view that a given shareholder’s objective function, actions, identity, and nature will differ greatly among different individuals. Therefore, according to Douma et al. (2006), Tihanyi et al. (2003), and Thomsen and Pedersen (2000), a given firm’s movements, performance, and approach may be significantly impacted by the varying actions and interests of the shareholders, so it is essential to establish what kind of shareholder is being dealt with at the time—whether that is a family, firm, lone individual, or entire government. After all, as we have seen, varying shareholders differ greatly in terms of their tendency to take risks, their usual income, and the importance they place on each involved individual’s values. These variable interests among different shareholders take us back to the core problem that ultimately breeds agency issues: the likes of investment aims, opportunities
for decision-making, and the offering up of resources, as these, according to Douma et al. (2006) establish individual aims, amount of control, and aptitude for monitoring managers. When the organisation’s key goal of value maximisation is no longer complemented by the organisation’s actions, conflicts of interest within the organisation tend to arise. Hence, as highlighted by Haji and Mubaraq (2015), shareholder interests will always, inevitably, influence owner preferences and investment decisions. An example of such a misalignment is presented by Rostami, Rostami, and Kohansal (2016), whereby stakeholders possess a wealth of aims that can jeopardise the simple need for stakeholders to perform as principals because they have dual roles (e.g., when banks are both lenders and owners).

To summarise, when it comes to establishing the problems associated with ownership concentration and the ways in which they can be solved, agency theory is essential—and, according to Shleifer and Vishny (1997), corporate governance can be one such solution. Indeed, it has been concluded that publicly owned firms are not as profitable as private- or mixed-ownership firms, even when such publicly owned firms are less reliant on debt (Abdallah & Ismail, 2017; Romano & Guerrini, 2014), and that agency costs can be reduced via good corporate governance operations (Hu & Izumida, 2009; Shleifer & Vishny, 1997).

Notably, in order to protect their needed cash flow, insurance and pension firms may be open to a fixed income, while capital gains would be of more interest to small shareholders. Further, declaring that family ownerships frequently invest in human capital that is more firm-specific, James (1999) also states that since family loyalty alone would be able to eliminate a wealth of issues, family-owned firms may control the firm completely. It is also worth noting that family-owned businesses are more likely to be wary of risks, since their firm performance and value is very easily swayed by any fluctuations in capital. In a similar vein, enhanced firm performance and reduced capital costs are common in organisations owned by the government; since they often prioritise durable investments, government-owned firms may find minority shareholders to be advantageous (Eckel & Vermaelen, 1986). Saying this, political and non-monetary objectives are likely to cloud the vision of government ownership holders, which has the potential to reduce firm performance.

Gulf businesses are often family-owned businesses and are identifiable by their high ownership concentration. It is our aim that the factors influencing firm performance within Kuwait will be better understood when the findings of this research on ownership structure are shared, since developed countries have seen higher investor protection and corporate governance than developing countries such as Kuwait. Notably, the goal of this particular section is to measure
the managerial ownership, the ownership’s identity, the ownership concentration of large shareholders, and their impact on Kuwait Stock Exchange-listed services and industrial businesses on the grounds of the agency perspective.

According to Fazlzadeh, Hendi, and Hahboubi (2011), ownership percentage substitutes the rights that would normally be included in the role (e.g., electing board of directors), so when it comes to examining firm performance, an essential element of corporate governance is the business’s ownership structure. This is because a firm’s ownership structure and the substituted rights greatly influence the overall operation of corporate governance, and thus play a vital part in establishing firm performance. Indeed, as has been noted by Fauzi and Locke (2012), a wealth of the current literature centres on developed countries’ firm performance and the influence that ownership concentration casts on this. As has been noted by Sikka and Stittle (2019) and Gillan (2006), shareholders and individual ownerships are reluctant to employ corporate governance code, so supervisory and monitoring functions are difficult to perform; yet, considering their power over scarce materials, only large investors are in a position to take up the role of ownership concentration (i.e., the proportion of shares possessed by a group of large investors [Saidat, Silva, & Seaman, 2019; Sanda, Mikailu, & Garba, 2010])—a role that essentially oversees and directs opportunistic management behaviours (Shleifer & Vishny, 1997). Family ownership, institutional ownership, foreign ownership, ownership concentration (explored above), managerial ownership, and government ownership are some of the tools for measuring ownership dimension that have been employed previously.

An ever-growing gap of shareholder information asymmetry can potentially occur via ownership concentration; large investors often take advantage of resources to meet their own wants, which frequently incurs negative repercussions (La Porta, Lopez, & Shleifer, 1999). Some examples of studies centred on the link between firm performance and the firm’s ownership concentration are those of Hu, Tam, and Tan (2010), Reyes and Zhao (2010), and Belkhir (2009b), who all noted a negative relationship between firm performance and ownership concentration. However, another three studies investigating the same topic (Azam, Usmani, & Abassi, 2011; Fauzi & Locke, 2012; Wang & Oliver, 2009) concluded that there was a positive relationship between firm performance and the firm’s ownership concentration. Meanwhile, Shah, and Hussain (2012), Najjar (2012), and Fazlzadeh et al. (2011) concluded that there was no clear relationship between these two factors.

The link between firm performance (i.e., ROA, ROE, and TQ) and corporate governance (i.e., audit committee characteristics, ownership structure, and board of directors’ characteristics) in
order to establish the ways in which these links may impact the future for a given firm (i.e., positively, negatively, or not at all). Notably, in a study investigating board size and CEO duality, the researchers concluded that the former greatly influences firm performance in the United Arab Emirates (Hassan & Halbouni, 2013). In a similar vein, another study measuring firm performance via $TQ$ and $ROA$ and corporate governance via governmental ownership, audit quality, institutional ownership, and board size concluded that these possess a positive relationship, apart from audit quality (Oasim, 2014).

In another study exploring these two factors in 435 non-financial publicly listed firms between 1999 and 2009, the researchers concluded that there was no link to be found between firm performance and corporate governance regulations (Akbar et al., 2016), which was supported by a variety of other research conducted within the field—notably, that which found a positive association between these two factors in organisations that were struggling to control their potential endogeneity.

Meanwhile, another prior study within the same field hypothesised that Malaysian firm performance and corporate governance characteristics would possess a mixed, or both a positive and negative, link (Haji & Mubaraq, 2015). The hypothesis was supported by their ultimate conclusions: both firm performance and independent chairs and non-executive directors possessed a negative association.

As can be easily seen from the above, the vast majority of the studies conducted within this field differ greatly in terms of results. Hence, we have attributed these differences to the following: these studies will have examined the datasets differently, with generalized least squares (GLS), robust and fixed effect regressions, or ordinary least squares (OLS); each of the samples was selected during different time periods; there were great cultural differences among the groups studied in terms of knowledge in the area, language, and their education; the market will have differed greatly for each study, as some will have been transition, developed, or developing markets; there were great monetary and political differences among the groups in terms of recent technological advancements, recent rebellions, and any financial crises; and finally, the groups’ judicial systems differed in terms of whether they employed civil law, a tribal system, or common law.

**Family Ownership and Firm Performance**

In order to properly comprehend corporate governance of ownership structures, we must first understand the ownership structure itself and then its degree of control and authority, because
international publicly listed firms are frequently very complicated (Augustine, 1998). Yet, as we have established via the current literature, ownership structure is an essential element of many firms, and thus vital to understand completely. Indeed, when we confirm that we fully understand the degree of authority and control for a given ownership structure, we are then in a better position to understand how shareholders can and may impact a given firm.

According to La Porta et al. (1999), managerial opportunism can be decreased if principals are better incentivised to govern agents because a high concentration of corporate ownership is allegedly abundant throughout the majority of countries, with the exception of the UK and the USA (Zhuang, 1999). Indeed, Gunasekarage, Hess, and Hu (2007) and Gürsoy and Aydoğan (2002) concluded that higher firm performance or general operational performance cannot necessarily be achieved through concentrated ownership.

Some researchers (i.e., Shleifer & Vishny, 1986) maintain that when the ownership structure is highly concentrated, shareholders can help alleviate agency issues, since they are incentivised and motivated to monitor managers, and they then attain more authority (meaning high ownership concentration would not have to be seen as a drawback and a negative influence on firm performance). Others, however, (e.g., Alchian & Demsetz, 1972) state that in order to alleviate such organisational issues, equity of ownership should be employed as a control mechanism—they claim that this can be proficient in establishing firm goals, managers’ levels of self-discipline, and shareholder wealth. In this case, it would seem apparent that more major shareholders would be preferable as a tool for governing and directing managers. According to Srivastava and Bhatia (2020), more major shareholders possess more motivation to closely oversee and govern managers—which, in turn, marks an unexpected positive result of having major shareholders that are largely concerned with their own interests. This notion is more commonly known as the shared benefits of control hypothesis and could be demonstrated in an instance of major shareholders controlling the selection of independent directors.

While it has previously been stated that a given firm can only be dubbed an official ‘family firm’ if upwards of 33% of that organisation’s shares are owned by that family (Barth, Gulbrandsen, & Schønea, 2005), others feel that this term can be attributed when the family owns upwards of 20% of voting rights (Faccio & Lang, 2002), while still others (Ang, Cole, & Lin, 2000) insist that a family firm is defined by their owning upwards of 50% of the firm’s stocks. Björnberg and Nicholson (2012) stipulate that if more than one family member fulfils an important position and that the family itself owns the largest business shareholding, they only then can be classed as a family business. Meanwhile, Claessens et al. (2000) and Morck,
Shleifer, and Vishny (1988) state that this term can be attributed to firms whereby the most important roles are fulfilled by the founder/in/direct relatives of the founder (either through marriage or blood), while Fahlenbrach (2009) and McConaughy et al. (1998) state that in a family firm those positions can only be held by the founder or direct relatives of the founder.

It could be pointed out that within firms where there is a higher likelihood of expropriation, major shareholders situated here would mean that such information would be unlikely to become widely known within the firm, and these firms typically possess minimal monitoring controls, since major shareholders would possess no motivation to do so. This is the stance taken by Jensen and Meckling (1976), who state that firm performance could be compromised because high ownership concentrations could lead to major shareholders only pursuing their own interests, and thus, taking advantage of the organisation’s materials. In this context, Jensen and Meckling (1976) maintain that expropriation is likely to occur in this scenario because major shareholders would be incentivised by the useability of several of the monetary components of their pursuits, as well as the gains they could obtain from monetary returns, for example when shareholders delegate all authority to their descendants (Bhaumik & Gregoriou, 2010). Notably, majority shareholders are able to undertake tasks that have the potential to completely undermine the requirements for good firm performance and minority shareholders, but that lead to benefits for them; they are also in a position to play all of the major roles within a given firm, wielding all the authority over the firm’s management and executive structure—all on top of the concentrated ownership they already possess. From this, we can see that concentrated ownership oftent facilitates instances of partiality within the workplace. Further, according to Demsetz and Lehn (1985), developing economies typically aim to form a ‘non-pecuniary income’ (e.g., the ability to allocate materials in accordance with one’s own wants) by employing majority ownership within large firms in the form of concentrations of power, such as in families. However, it has been noted that the negative repercussions of agency theory (i.e., conflicts of interest between principals and agents) can be alleviated through family ownership (Purkayastha, Veliyath, & George, 2019; Srivastava & Bhatia, 2020).

According to Anderson, Mansi, and Reeb (2003) and Demsetz and Lehn (1985), the general reputation of controlled/family-owned organisations (i.e., where the organisation’s durability and ability to flourish is the utmost priority) can help alleviate outside debt and equity agency costs. Furthermore, according to Peng and Jiang (2010), Suto (2003), La Porta et al. (2000), and Shleifer and Vishny (1986), in instances where a developing country’s subpar legal protection is replaced by shareholders, these countries’ firms can in turn see better performance.
as a result of improved equity concentration. Indeed, such a notion aligns with the separate idea that minority shareholders are advantageous for Western European family-owned firms, rather than being damaging to them (Maury, 2006). It is essential to bear in mind that the very foundation of any family-owned firm is a familial ‘binding’ (Litz, 1995) and spirit (Fama & Jensen, 1983b), and that the family’s very characteristics are what will ultimately determine the firm’s inner workings (Mishra, Rondoy, & Jensen, 2001). According to Burkart, Panunzi, and Shleifer (2003), such elements make any family business a good rival for any other similar firm.

Both large and small family-owned firms are essential within GCC countries’ overall economy (Chang, 2003; Joh, 2003), and, according to Claessens et al. (2000) and Johnson et al. (2000), GCC sit on top within many developing nations. However, there are assorted results when it comes to determining whether family-owned businesses perform better than other businesses or not. Nowland’s (2008) and Morck et al.’s (1988) empirical research results indicate that firms that are family-owned tend to perform less well than firms that are not, while Demsetz and Villalonga (2001) and Demsetz and Lehn (1985) maintain that there is no notable difference in performance between the two. Meanwhile, Margaritis and Psillaki (2010), Villalonga and Amit (2006), Maury (2006), and Anderson and Reeb (2003) state that family-owned firms in developed countries tend to perform better than their non-family-owned counterparts.

According to Jensen and Meckling (1976), the agency problem concerns the fact that the control and ownership at play facilitates concentrated shareholders to trade private rent profits—and this has become known as a massive issue within family-owned corporations. In line with this, the current literature focusing on family-owned firms will often direct attention to these drawbacks, and then draw conclusions along the lines of family-owned corporations not being very lucrative or effectual. An example of families who run businesses undermining shareholders in pursuit of their own interests is put forward by Demsetz (1983), whereby these family members extract limited materials from lucrative projects to instead further their own ‘non-pecuniary income’. Carne (1998) extends this example by pointing out that family shareholders have the ability to allocate the important roles within their business only to their own family members; hence, they prioritise family loyalty over professionality or their staff members who possess the right skillsets or qualifications to do so. Indeed, Shleifer and Vishny (1997) add that family shareholders tend to regard their business as a sort of private bank or free place for relatives to work, rather than a professional, unbiased, working business. Hence,
according to Martínez and Requeio (2017), Gomez, Nunez, and Gutierrez (2001), and DeAngelo and DeAngelo (2000), firms that have large and undiversified owners or CEOs will frequently perform worse than firms that possess a dispersed ownership structure.

As stated by Davis et al. (1997) and Fox and Hamilton (1994), stewardship theory undertakes varying psychological and situational precursors to individual behaviours, and has become increasingly prominent within studies concerning family-owned businesses. Jaskiewicz and Klein (2007) and Lane et al. (2006) have pointed out that, because matters of ancestry are highly relevant for employees and manager(s) within family-owned business, stewardship theory is particularly important within family-owned businesses whereby managers act as stewards, which leads to their use of more mindful, considerate behaviour—something that stands in stark contrast to the self-interested nature of agency theory. It is also particularly relevant because, as pointed out by Pieper, Klein, and Kaskiewicz (2008) and Davis et al. (1997), matters of whether incentives are aligned among principals and agents have little relevance in family-owned firms—making redundant the whole premise of applying agency theory to such businesses. Indeed, a wealth of research within this area concludes that family-owned firms tend to perform better than non-family-owned firms. For example, McConaughy et al. (1998) found that non-family-owned firms performed worse than their family-owned counterparts in terms of stock market returns and market-to-equity ratios. Similarly, a study in 2003 concluded that S&P family-owned businesses beat their non-family-owned counterparts in market value by 10% and ROE and ROA by 6.65%. Furthermore, in another study conducted in 2003, the overall conclusion drawn was that, when legal security within a given family-owned business is moderate or low, and the arising agency issues are too extreme to facilitate any distinction between management and ownership, it would be most beneficial to the business for the family members to stay on-board (Burkart et al., 2003). In the same vein, an investigation of Fortune 500 firms concluded that there was a positive relationship between managerial ownership (via $TQ$) and firm performance (Morck et al., 1988). The 2006 study that examined control, management, and ownership within family-owned businesses is an example of an Asian/European-based study identifying a positive link between high firm performance and businesses being family-owned; the researchers concluded that there was a negative relationship between firm performance and a descendant of the founding family member filling the CEO role, although they also concluded that when this position was fulfilled by the founding family member, firm performance was enhanced. This result can likely be explained by the descendant possessing less incentive for running the business well than the
founder (Villalonga & Amit, 2006). Another study similarly concluded that there was a positive relationship between firm performance and a high income and family ownership, once nation effects, industry, and capital structure were controlled for (Thomsen & Pedersen, 2000). Furthermore, a 2004 study concluded that there was a positive relationship between net income-to-sales and ROA and family ownership in Thailand (Yammeesri & Lodh, 2004). Meanwhile, the nature of the relationship between leverage ratio and family ownership has most certainly not gone without investigation. As an example, Palmberg (2015) outlined that there was no notable link between firm performance and ownership concentration and family ownership within Swedish family-owned businesses. Meanwhile, Santos, Moreira, and Vieira (2014) outlined that there was a positive relationship between leverage ratio and family ownership within the 694 Western European firms they investigated.

In a similar vein, the performance of firms within GCC countries and how and whether they are affected by family ownership has been a great area of research. One survey conducted in 2017 concluded that the vast majority of more than 100 family-owned businesses in the GCC region reported that corporate governance was a lower priority to them than some of the other challenges within their businesses, such as their total income and their commercial and functional worries, although these business owners also acknowledged that corporate governance was essential to ensure the durability of their business (Abdallah & Ismail, 2017). Indeed, more and more GCC business owners are recognising that good corporate governance is necessary to ensure the durability of family-owned businesses—but it is not yet considered to be a strategic priority within these regions, even though, with the exception of the oil industry, the GCC economy is largely supported by family-owned businesses, which produce an estimated 80% of its annual GDP. In line with this, it has been noted that family ownership is generally acknowledged to be the more popular form of ownership within developing nations (Yang, 2010).

In a similar vein, within a study conducted in 2014, it was concluded that firm performance and family- and institutionally owned GCC banks possessed a positive relationship, while the factors of CEO duality, government ownership, or board size showed a negative relationship within such firms (Arouri, Hossain, & Badrul, 2014). Notably, corporate governance within family-owned GCC corporations faces the hurdles of solving conflicts, formalising management structures, enhancing board operations, the matter of who will be appointed to certain roles next, and ensuring that culpability and honesty are maintained. Notably, countries such as Kuwait that are situated in the GCC region often find corporate boards are not the most
beneficial to employ—and, in line with this, the topic of ownership composition (e.g., involving individuals, governments, or institutions, and their influence over the given firm’s performance) in the context of Kuwaiti firms is necessary. Therefore, the main bulk of this study concerns the nature of the association between firm performance and ownership concentration within such firms.

Institutional Ownership and Firm Performance

Institutional ownership has been widely researched and influences all firms within both developed and developing nations. Fazlzadeh et al. (2011) defined institutional ownership as a form of ownership structure and the percentage of stocks possessed by the firm itself compared to the total stocks. Notably, it has been pointed out that, because of their desire to protect equity investments, institutional investors are inherently incentivised to oversee and correct any actions made by managers—meaning that they positively influence firm performance (Shleifer & Vishny, 1986). In a similar vein, firms are expected to greatly influence the overall network of corporate governance (Cornett et al., 2007)—and institutional investors are highly influential in ensuring good corporate governance. Finally, Kansil and Singh (2018) noted that corporate governance can aid communication between the firm and individual investors.

When it comes to the expansion of the capital market, institutional investors have grown in essentiality—and with this essentiality, their abilities as shareholders have similarly expanded. In this vein, Gillan and Starks (2000) pointed out that, alongside pension assets’ development, firms centred on insurance, foundations and pensions, investment, and bank trust are extremely prominent and influential within the equity market; thus, their involvement in equity ownership has risen rapidly.

The wide scope of literature that investigates institutional ownership as one internal mechanism of corporate governance (whereby they function in the key invested firms [Annuar, 2015; Mizuno, 2014]) frequently outlines the fact that institutional ownerships add to the relevant business’s corporate governance when they are actually functioning. In this context, it has been highlighted that institutional ownership can actually ultimately enhance firm performance by checking for managers’ opportunistic behaviours (Mokhtari & Makerani, 2013). It has also been noted in a wealth of research in this area that institutional ownership and firm performance share a positive relationship, since (as capital structure and institutional development possess a negative relationship) areas that are institutionally better positively influence their own cash flow and control rights. Such a notion is explored in a study conducted in 2013, which concluded that the institutional quality matters most when limiting the expropriation displayed
by owners (Su, Wan, & Li, 2013). Furthermore, yet another study surmised that as long as firms continue to participate in social pursuits, they will always be able to appeal to and keep institutional owners (Saleh, Zulkifli, & Muhamad, 2010). Finally, corporate monitors (i.e., institutional owners, should they take up such a role) and the wealth of research concerning them (e.g., Grossman & Hart, 1980; Shleifer & Vishny, 1986) conclude that such monitoring occurs when large stakes are placed in the invested-in firms, since such stakes comprise the ability to direct, sway, and oversee managers, as well as the materials and opportunities within business.

The results surrounding this area of study are rather mixed. According to Tahir (2015), Tornyeva and Wereko (2012), Chen, Blenman, and Chen (2008), and Cornett et al. (2007), the positive influence of institutional ownership over firm performance urges firms to safeguard shareholder interests and implement good corporate governance. Meanwhile, a wealth of other studies noted both a negative and positive relationship between firm performance and institutional ownership (Afza & Nazir, 2015; Fazlzadeh et al., 2011; Homaidi et al., 2019; Irina & Nadezhda, 2009).

Alfaraih, Alanezi, and Almujamed (2012) consistently found that while some types of owner will enhance firm performance, other types will most certainly reduce it. In Mizuno’s (2014) study, it was loosely concluded that institutional investors often base their decision on anticipated ROE performance when they are selecting firms to invest in, since enhanced firm performance was witnessed among the groups with the biggest increase in institutional investor ownership. Furthermore, a 2014 study found that firm value and managerial ownership, firm performance and director compensation, and firm performance and ownership concentration all possessed a positive relationship, while a negative relationship was documented between firm performance and debt financing and firm performance and director compensation (Du, Chen, & Shao, 2014). Furthermore, yet another study highlighted that there was a negative relationship between corporate value and foreign institutional ownership and a positive one between firm performance and domestic institutional investors (Thanatawae, 2014), so we can comfortably conclude that there is a positive relationship between firm performance and institutional ownership.

In the same vein, it has been concluded in a 2001 study that foreign institutional investors’ holdings and firm performance in Sweden possess a positive relationship (Dahlquist & Robertson, 2001). Similarly, another study concluded that there was a positive relationship between institutional investors’ percentage ownership and $TQ$ (McConnell & Servaes, 1990).
In contrast, a study conducted in 2018 concluded that there was a negative relationship between firm performance and institutional ownership within mainland Chinese firms (Ali, Qiang, & Ashraf, 2018), while another concluded that there was a positive link between firm performance and institutional ownership within Pakistani firms between 2008 and 2013 (Tahir, 2015). A study conducted in 2001, on the other hand, concluded that there was no identifiable relationship between firm performance and ownership structure within US firms (Demsetz & Villalonga, 2001). This conclusion is supported by Chung et al. (2008), who similarly concluded that there was no identifiable relationship between firm performance and institutional investors. Notably, there seems to be a neutral link between the lucrativeness of north-eastern Chinese firms and institutional ownership, while these same firms saw a negative relationship between ROA and institutional shareholding.

There are, admittedly, fewer studies on the relationship between institutional ownership and firm performance in GCC countries than those studying this relationship in non-GCC countries. Nonetheless, such studies do exist. A positive relationship between bank performance and foreign, family, and institutional ownership was noted in a study conducted in 2014, although no identifiable relationship between firm performance and government ownership was seen in the 58 studied GCC banks (Arouri et al., 2014). Similarly, while no identifiable relationship between firm performance and foreign and institutional ownership was noted here, Zeitun (2014) did document a positive relationship between firm performance and ownership concentration, government ownership, and ownership structure within GCC markets. In contrast, a 2015 study concluded that there was no identifiable association between major institutional shareholders and firm performance within non-financial firms based in Kuwait (Al-Saidi & Al-Shammar, 2015). Such a different result from the other studies in this area may be caused by the difference in time period of conduction, since corporate governance codes alter between different eras.

We could hypothesise that firm performance could be enhanced with by implementing high ownership concentration, since high proportion of institutional ownership can closely oversee managers and substitute for lacklustre corporate governance. Conversely, we could postulate that such implementation would lead to reduced firm performance, since a high amount of intrusion into managers’ decision-making could have a negative impact on the decisions made, particularly in cases where the ownership is looking for private control benefits. Regardless, based on all of the above, we can comfortably conclude that firm performance is impacted differently depending on the different concentration levels of institutional ownership that are
employed. In light of Jameson, Prevost, and Puthenpurackal’s (2014) conclusions (i.e., that firm performance and dual firm investors and controlling shareholders possess a positive relationship within Indian firms), and those of the other studies discussed (i.e., mixed results), we conclude with a non-directional hypothesis: that there is a significant relationship between firm performance and institutional ownership, but that we cannot predict the direction of such a relationship. Furthermore, I conclude that opportunistic behaviours in managers and agency costs can both be reduced by implementing major institutional investors, since they possess an abundance of experience and knowledge in fulfilling the role of a supervisor well, although this will not entirely eliminate the possibility of institutional investors attempting to sway how materials are utilised.

**Government (State) Ownership and Firm Performance**

As pointed out by Laidroo (2009), decision-making within firms and corporate governance disclosure are greatly impacted by government ownership within developing countries where not all firms are wholly privatised, meaning that the government will often place large investments in its firms. Furthermore, we can say that firms are likely to be incentivised to be more transparent with their corporate governance operations as a result of conflicts of interest between shareholders and managers, as well as political control by government stakeholders. The state is responsible for a great wealth of stakeholders, so the government may insist on firms being more transparent with such information (Ghazali & Weetman, 2006). Furthermore, firms seeking to reduce manager-shareholder conflicts of interest need to offer more insight into their corporate governance operations. Otherwise, they will likely face higher agency costs. This necessity arises because shareholders’ interests are not always of utmost importance within a given firm, since many governmental businesses possess non-pecuniary objectives and their own profit shares (Eng & Mak, 2003).

Notably, considering the state is somewhat pressured to act as a large and longstanding investor, the corporate control market may not be the most effectual in governing directors and managers, as a result of related political intrusion when these individuals are selected. In a similar vein, Eng and Mak (2003) found that, since they depend on the state more than any other entity for required investment, firms with several government shares are better positioned to obtain the monetary materials they require. Such dependence can potentially dissuade firms from being transparent with their corporate governance, since they can increase external funds with ease and at whatever rate they please.
A wealth of the research within this area (and it has, indeed, been a topic of much exploration within the field) has concluded that firm performance can be significantly swayed by government ownership when paralleled with other global versions of ownership concentration. However, government ownership has been put down as a sedentary resource when it comes to trying to enhance firm performance within developing nations (e.g., Ting & Lean, 2015). Further, it has been concluded that businesses that possess a great amount of government ownership typically receive higher funds (Pan et al., 2014). Indeed, this notion is backed by the widely accepted view that other ownership types do not offer nearly as much admission to finances as government ownership does.

The results from research conducted into whether government ownership positively or negatively impacts firm performance are largely a mixed bag—which may result from the wide variety of nations being studied. For example, while it is understood that the negative link between firm performance and government ownership should not be oversimplified, it has been stated that firms will be less motivated to utilise good corporate governance because of their easy access to any required funds and the low amount of accountability maintained within government-owned firms’ pecuniary performance (Mak & Li, 2001). Indeed, the likes of Mak and Li (2001), Miggenson and Netter (2001), and Xu and Wang (1999) found that government ownership has a negative impact on firm profit and efficiency compared to privately owned firms, implying that, overall, there is a negative link between firm performance and government ownership. It is noted that, because governmental investments are usually directed towards enhancing social wellbeing rather than maximising the firm’s profits, firm performance and government ownership possess a negative relationship; the work of Mak and Li (2001) is an example of Singaporean evidence. Similarly, yet another investigation into the nature of the relationship between these two factors suggested there was a negative relationship between firm performance and government ownership within Chinese organisations (Xu & Wang, 1999). Meanwhile, another investigation into this area concluded that European firms with high amounts of government ownership have fewer accounting needs because they are protected by the government, and vice versa, and that this is because such firms were found to be more liberal in their approaches than their counterparts with low government ownership (Gaio & Pinto, 2018). Furthermore, while in this case there could be a non-linear relationship between ownership structure and firm performance, in yet another study in this area a negative relationship between firm performance and government ownership was noted for Jordanian firms (Zeitun & Tian, 2007).
Conversely, the below researchers noted that firm performance and government ownership possessed a positive relationship, including Alfaraih et al. (2012), Aljifri and Moustafa (2007), Ang and Ding (2006), and Najid and Abdul Rahman (2001). Indeed, a positive relationship between firm performance and government ownership was noted within a study exploring the link between firm performance and the amount of shares held by the government within 514 privatised Chinese firms (Liao & Young, 2012). Similarly, Aljifri and Moustafa (2007) concluded that managers of government-owned firms may be incentivised to make accounting decisions that would ultimately improve firm performance as a result of the lack of pressure they face to act in accordance with financial reporting regulations, since such firms have easier access to their pecuniary needs than other firms, and they tend to have the issue of asymmetric information alleviated (Eng & Mak, 2003). Furthermore, a positive relationship between Oman firm performance and government ownership and ownership concentration was noted within a study measuring these factors with the aid of multiple regression analysis and examination of ROA, likely because the government is highly proficient in governing in-firm operations (Al-Matari & Al-Arussi, 2016). In contrast to this, however, Shleifer and Vishny (1997) pointed out that the government is typically more interested in pursuing its own socio-political goals than those of the firm, so government ownership would surely be less effective than other types of ownership.

In light of all of the above, it seems fair to hypothesise that there will be a positive relationship between Kuwaiti firm performance and government ownership because the Kuwaiti Government very actively champions any rules and regulations that ensure the safeguarding of investors for Kuwaiti financial markets. Going on from this, there is also an anticipated positive relationship between Kuwaiti firm performance and government ownership and corporate governance, since the Kuwaiti Government is somewhat renowned for its high degree of honesty in terms of its corporate monitoring. Indeed, such a notion is backed by a wealth of studies, including one that concluded there was a positive relationship between Chinese firm performance and government ownership due to its government’s consistent investment in high-performing firms, which provides advantages from both a political and an economic perspective (Ng, Yuce, & Chen, 2009). Notably, it has been stated that several factors that vary with each nation, such as path dependence and government quality, will impact firm performance differently (La Porta et al., 1999). Moreover, it was concluded in 2015 that Islamic banks possessed a positive relationship between firm performance and governance quality (Srairi, 2015), while another study found the same conclusion for its 24 studied GCC banks.
(Naushad & Abdul Malik, 2015). Finally, surmising that government-owned firms are more supported and safeguarded financially than those with other ownership structures.

### 4.3.2 Boards of Directors’ Characteristics and Firm Performance

As detailed by Liu and Fong (2010), as the board possesses more control, managers receive fewer opportunities for tasks that would increase shareholder value, the most important of which is to oversee agents’ management and ensure it aligns with shareholders’ interests. Boards are flexible in terms of how they are structured, as they can be designed in line with the firm’s goals, and they mark the top of the pyramid of control systems. A wealth of opinions within research have been expressed concerning the structuring of a board, that the like of Liu and Fong (2010) and Fama and Jensen (1983b) being that the variations between the interests of managers and shareholders can be minimised through a board structure that needs constant oversight of managers and approval by external directors. The likes of Earnhart and Rassier (2016) and Black et al. (2015) expressed the opinion that increased firm performance could be attained by structuring the board in a way that facilitates management control of the board, since this would increase the independent directors’ understanding of the firm’s requirements. According to La Porta et al. (2000), considering that performance is increased and risks minimised via suitable governance structures, external investors acknowledge that corporate governance is a factor that has much influence over investment decision-making.

Furthermore, according to Petra (2007), while the two above perspectives concerning board structure seem to be other polarising, it is important to remember that the vast majority of firms will implement structures that strike a balance between the two above perspectives, including external director monitoring and managerial control.

Hence, as acknowledged by Baranchuk and Dybvig (2009), Gillan (2006), and Fama and Jensen (1983b), the board of directors is in a position to oversee and approve vital decisions, to guarantee that executive directors are, indeed, acting in accordance with principals’ interests, and to send away, reimburse, and occupy head managers. As stated by Aguilera and Cazurra (2009), resource-dependency theory acknowledges the board of directors as a co-optative device tasked with standardising the firm in terms of outside environmental pressures, so we can see that agency theory solely depends on a very simplistic comprehension of human behaviour in the context of forming contracts and business-related agreements. Indeed, as outlined by Fama (1980), agency theory acknowledges that boards of directors are the individuals required to offer the best approach for obtaining effective and reliable corporate governance, and are thus seen as essential in the process of manager decision-making. Here, a
key issue that requires further attendance in the context of board structuring is the suitable reimbursement and selection of directors (Keasey, Thompson, & Wright, 2005). To set about solving this concern, good communication among shareholders and board members, transparency, sufficient logic to fix monetary issues, recurrent meetings, open-mindedness concerning others’ suggestions, attentiveness and concern over pecuniary problems, and acting in accordance with what is best for the business, should all be implemented within board construction (Solomon, 2010).

Services, control, and resource dependence are the three categories into which directors’ roles can fall. According to Johnson, Daily, and Ellstrand (1996), the first comprises directing the CEO and any leading managers about any managerial problems, and advising these figures when creating approaches for the organisation going forward. The control role, according to Horrigan (2007), comprises ensuring that managers act in accordance with shareholders’ interests, and is burdened with the task of dismissing and hiring the CEO and the managers. Meanwhile, as outlined by Pfeffer and Salancik (1978), the resource-dependence role essentially comprises reaching out to outside relations in order to attain further materials for the firm’s success.

A study conducted in this area concluded that safeguarding of investors would be increased by implementing the characteristics of the board of directors (e.g., director independence within meetings) (Liu, Wang, & Wu, 2016). Another study examined the relationship between firm performance and board size in relation to shareholder returns and concluded that the Gini coefficient is the most helpful in establishing executive pay inequality and corporate performance (Forbes, Pogue, & Hodgkinson, 2016). Notably, when it comes to maintaining their task of overseeing (with the ultimate aim of substituting inefficient CEOs with better performing ones), it is essential that directors maintain their independence, since it has been noted that internal directors are further incentivised to monitor CEO actions when the director in question is independent (Hermalin & Weisbach, 1988). Furthermore, it has been suggested that in order to solve issues between the CEO and the board, the vast majority of board members should adopt the role of non-executive directors (NEDs), since this is an independent role, as well as a mediating one (Fama & Jensen, 1983b). Furthermore, conflicts of interest between shareholders and managers can be reduced by improving the monitoring of managers, since this increases the likelihood that managers will act in accordance with shareholders’ interests.

A great wealth of research within this area has been entirely dedicated to the topic of the relationship between firm performance and boards of directors, and seeing how other works
within this area compare. One such study concluded that the performance of the 634 studied UK firms was moderately impacted by board structure (El-Faitouri, 2014), while two other studies (Adams, Hermalin, & Weisbach, 2010; Ullah & Kamal, 2020) concluded that much of the literature within this area would be better classed as united reports of the relationship between firm performance and board structure, and of the process of appointing directors. Corporate governance implies that firm performance is expanded by its associated mechanisms, so in addition to the aforementioned results, El-Faitouri (2014) concluded that there was no identifiable relationship between firm performance and board of directors’ characteristics. In light of all of the above, the following subsections elaborate on board meetings, board outsiders, board size, and board independence, and their relation to firm performance.

**Board Size and Firm Performance**

As maintained by Hoseini, Safari, and Valiyan (2019), Nkundabanyanga, Tauringana, and Muhwezi (2015), Germain, Galy, and Lee (2014), and Sanda, Garba, and Mikailu (2011), the board of directors is an essential corporate governance mechanism when it comes to marrying the interests of shareholders and managers. This is because, as stated by Adams and Ferreira (2007) and Raheja (2005), monitoring and advising are the two most important roles of the board of directors. As suggested by Lawal (2012), it is possible that firm performance, monitoring, and decision-making could all be improved by adopting a small board size, as this was seen to encourage an authentic, informed, and essential style of communication between members. Notably, maintaining a good relationship between managers and stakeholders and monitoring the firm’s and CEO’s activities are the two key roles of a board (Zahra & Pearce, 1989).

A range of different researchers have different opinions regarding how many board members is most desirable to promote the best possible performance: Brown and Caylor (2004) argue for between six and 15, while Jensen (1993) insists on between seven and eight. Meanwhile, Cadbury (1992) argues for between eight and 10, half going to NEDs and the other half going to executive directors. Further, while between eight and nine members is desirable to Lipton and Lorsch (1992), in stark contrast, Dalton and Dalton (2005) maintain that large boards facilitate more opinions and discussion, hence enhancing the diversity within a given firm and providing different perspectives in decision-making. Notably, in the context of Kuwait, Kuwaiti firms are known to adopt upwards of five board members.
Indeed, the efficiency and capabilities of a given organisation can be predicted by the structure and size of the board within it, the impact of the latter materialising in the form of participation and engagement within tasks and business matters. Indeed, when it comes to implementing good corporate mechanisms, board size is an essential factor. Indeed, the likes of Singh and Davidson (2003) and Hermalin and Weisbach (2001) advocated for a smaller board size, and McKnight and Weir (2009) stated that a small board size results in lower agency costs. Maintaining that managers have a tendency to grow a board size past its highest point of value, one researcher stated that a larger board size compromises firm value because new incompetence performs well in terms of coordination, overseeing, and communication—hence, they suggested a board size of 10 or fewer members (Jensen, 1993). Furthermore, yet another researcher concluded that smaller boards of US firms showcased a higher TQ after it was found that US firms with larger board sizes showcased subpar coordination, monitoring, and communication. Agency theory also backs this notion that larger boards are inefficient: it assumes that agents tend to construct large boards, which are ineffective, and so concludes that there is a negative relationship between firm performance and a large board. However, it was concluded in another study that the secret to building an effective board is taking enough time to ensure diversity is attained—hence, prior literature maintain that there is no one number of board members that needs to be reached in order for them to be effective (Conger & Lawler, 2009).

The influence cast by board size varies with each area, according to whether they are pecuniary or accounting problems—and, in line with this, a wealth of research has been conducted within this area. One such study concluded that accumulating more debt in order to minimise agency problems negatively influences corporate governance within Nigerian firms (Ranti, 2013). Similarly, another study concluded that large boards with a larger temporary debt-to-assets ratio tend to possess an equity premium, while those with more long-term debt usually possessed an equity discount (Upadhyay, 2015). Furthermore, other research concluded that there is a negative relationship between board size and corporate risk (Haider & Fang, 2016).

A related study documented a positive relationship between board size and firm performance within the studied Pakistani firms (Latif et al., 2013); another study noted the same result for the studied US firms (Adams & Mehran, 2008). However, another analysis documented a negative relationship between firm ROE and TQ and board size (Guest, 2009), and another offered the one-tailed conclusion that there is a significant relationship between firm performance and board size (Zahra & Pearce, 1989).
Conversely, a subsequent analysis into Malaysian board sizes and firm performance concluded that there was no identifiable relationship between these two factors (Fooladi & Nikzad, 2011), and another study conducted some years before offered a similar conclusion: that there was no identifiable relationship between firm performance (measured via $TQ$) and board size (Aljifri & Moustafa, 2007). Notably, the works of Loderer and Peyer (2002), Conyon and Peck (1998), Eisenberg et al. (1998), and Yermack (1996) support the notion that the ‘free-rider’ issue can be exacerbated by a large board size, as was also outlined by Kajola (2008).

According to Hillman and Dalziel (2003) and Dalton et al. (1999), board size is intrinsically related to the firm’s ability to gain admittance to required materials and outside individuals; therefore, it has been suggested that more resources can be accessed with a larger board (Farag & Mallin, 2019; Hillman, et al., 2001). To support such a notion, an investigation conducted in 1991 surmised that a corporate identity and corporate relationships can be expanded with the aid of a large board size (Pearce & Zahra, 1991). To go along with this, yet another study documented the existence of a significant relationship between Tobin’s $Q$ and board size within the 348 studied Australian firms (Kiel & Nicholson, 2003). In contrast, another set of researchers reported that there was no identifiable significant relationship between firm performance and board size (Connelly & Limpaphayom, 2004). Meanwhile, another study centred on this relationship concluded that there was a potential positive relationship between efficient advising and monitoring of managers and firm performance/value and board size within the banking sector (Andres & Vallee, 2008). Finally, yet another study in this field documented that there was not an identifiable relationship between firm performance and board size for firms situated in the United Arab Emirates (Aljifri & Moustafa, 2007).

A study conducted in 2013 documented the existence of a negative relationship between firm performance and board size within the banking industry (Al-Saidi & Al-Shammari, 2013). Similarly (and in turn suggesting that there is a negative relationship between firm performance [measured via $ROA$ and board size], it was concluded in a separate investigation that board size had a negative but unimportant impact on firm performance (Al-Matari et al., 2012a). In contrast, the findings of another study (i.e., that there was a positive relationship between firm performance and board size within Kuwaiti firms across all measuring tools) implied that, when it comes to improving firm performance, large boards are better equipped in terms of materials and skillsets and, thus, would be better for decision-making (Al-Shammari & Al-Sultan, 2009). Hence, it could be concluded from the above that, in order to enhance firm performance within Kuwait, these firms should enlarge their boards. But then again, considering the first
aforementioned research results, it may be more suitable to conclude that the nature of the relationship between firm performance and board size is largely variable—possibly as a result of temporal differences, and/or possibly as a result of insufficient corporate governance practice.

It is important to remember that each theory within this area possesses factors that can be employed within different circumstances, despite Kiel and Nicholson’s (2003) statement that there is not one single theory that has the potential to comprehensively explain the nature of the relationship between firm performance and corporate governance. Indeed, as noted by Dalton et al. (2003), the greatly varied findings within the aforementioned studies at least ascertain that there is unlikely to be any unanimous opinion concerning the board size that would be most beneficial to employ. Suggesting that the relationship between firm performance and the different types of corporate governance may be highly reliant on the circumstances in which such a relationship was to occur, Rajangam, Sundarasen, and Rajagopalan (2014) concluded that while bad firm performance could be a result of the board’s structure, the way in which the firm grows could be influenced by board size.

**Board Meetings and Firm Performance**

Hahn and Lasfer (2016) and Al-Najjar (2012) have made the point that the directors’ ability to attend frequent meetings so as to improve their monitoring skills will be reduced via the expressed disapproval of such directors—which, in turn, strengthens the view that board meetings are a resource. Furthermore, according to Vafeas (1999), board meetings can be classed as a pertinent board resource that can measure the strength of the operations ongoing within the board. Implying that in order to avoid having to make any such costs, there is a particular number of board meetings that should take place, Vafeas (1999) also stated that travel, managers’ time, and directors’ fees are all elements of board meetings that incur financial costs—something pivotal to acknowledge among the many benefits of board meetings, such as the fact that they provide opportunities to establish approaches, oversee managers, and talk about any issues within the firm. Furthermore, it has been found a number of times within the literature investigating this topic that directors tend to actively complete activities that they know will enhance firm performance when they attend regular board meetings. According to a study by Lin, Yeh, and Yang (2014), board meetings are pivotal for ensuring the effective execution of in-board errands—as is the board process as a whole. Such a notion is supported by the conclusions of yet another study, whereby it was proposed that board meetings are essential for enhancing the success of the board (Conger, Finegold, &
Lawler, 1998). In line with this, another set of researchers supported that too little time available to complete board operations had a massively negatively impact on firm performance (Lipton & Lorsch, 1992). To sum up the aforementioned conclusions more comprehensively, Vafeas (1999) went on to document that there is a strong relationship between firm performance and board meetings, the latter of which is also documented here as advantageous to some of the other elements of board success. As an example of this, a study conducted in 2000 concluded that there was a positive relationship between involvement in fraudulent activity and irregular attendance at audit committee meetings (Beasley et al., 2000). To support such a conclusion, another study conducted some years later documented the existence of a relationship between the quality of audit work and the frequency of board meetings. In stark contrast to such conclusions, Jensen (1993) maintains that when boards encounter issues, they need to become active, and, when they do not, they should be inactive. , Jensen (1993) also maintain that time constraints mean directors cannot share any significant information, so board meetings are not particularly needed. This view is also supported by Lipton and Lorsch (1992). Indeed, when this matter is examined from the perspective of agency theory, it becomes evident that managerial monitoring will be improved when boards are more conscientious about assigning tasks to different members. Despite the fact that the number of board meetings is the only accessible public data, it has been admitted within a study that focus within meetings, discussions after meetings, pre-meeting planning, and meeting involvement are some of the factors of board diligence in addition to board meetings (Carcello et al., 2002). Furthermore, it has been concluded within a study that boards should evaluate their own performance frequently and should put aside enough time to have a detailed conversation about any problems that have been encountered, thus indicating that firm performance could be improved by improving the monitoring of management.,

One study in this area concluded that there was a negative relationship between Italian firm performance and managerial ownership from the lens of agency theory (Greco, 2011). In contrast, another investigation concluded that there was a positive relationship between firm performance (in terms of ROA and ROE) and regular board meetings for the 118 studied Australian organisations (Hoque, Islam, & Azam, 2013). Vafeas (1999) documented the existence of a relationship between firm performance and board meetings and their result indicates that there is a significant relationship between the firm’s future performance and extreme monitoring, and a positive relationship between suitable decision-making and frequent conversations between directors. From this finding (i.e., this relationship between firm
performance and board meetings) we could also infer that some issues regarding endogeneity are at play here, because although enhanced firm performance may occur at the same time as an increase in board activity, such operations may have been increased due to bad firm performance. Regardless, the findings of another study conducted in 2018 support those of Vafeas (1999), as the researchers similarly concluded that there was a notable relationship between firm performance and board meetings (Mishra & Kapil, 2018). In a similar vein, another study noted a positive relationship between firm performance and board practices (Lawler et al., 2002), while Beasley et al. (2000) observed that there was a negative relationship between in-firm fraudulent activity and minimal audit committee meetings. One investigation conducted in 2004 concluded that there was no identifiable significant relationship between in-firm fraudulent activity and frequency of board meetings (Uzun, Szewczyk, & Varma, 2004); however, Vafeas (1999) documented the existence of a very strong negative relationship between firm performance ($TQ$) and frequency of board meetings. It is worth noting here that, from the lens of agency theory, monitoring managers to alleviate any manager misconduct and avoidable costs is the main role of any board. As a whole, it is generally agreed that board meetings are essential for ensuring board diligence, and studies such as those of Lawler et al. (2002) (which concluded that a positive association existed between firm performance and suitable board operations) support such a perspective.

A wealth of the current literature has centred its investigations on the link between firm performance and board meetings within the GCC region. One such study conducted in 2014 concluded that there was a positive relationship between Oman firm performance ($TQ$) and board meetings (Al-Matari, Al-Swidi, & Fadzil, 2014b), while another study observed the existence of a negative relationship between Bahrein firm performance ($ROE$) and board meetings (Aktan et al., 2018).

When examining all of the above investigations and their outcomes, it is noticeable that some were actually conducted before the implementation of corporate governance became widespread. Thus, there are clearly some gaps in logic and a lack of validity in some of the conclusions drawn.

**Board Independence and Firm Performance**

Board independence can be defined as instances where there are NEDs within the board of directors; these NEDs are advised by the code of best practice to be both independent. Furthermore, the combined code (2008) defines independent directors as follows:
The Board should determine whether the director is independent in character and judgement and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director’s judgement. The Board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination. (p. 8)

Considering that boards are required to be able to oversee and sway the decision-making and operations of managers, a wealth of codes of governance have voiced their own recommendations for a minimum amount or percentage of independent directors on a given board. As outlined by Jensen and Meckling (1976), external directors and/or NEDs have the ability to aid in the overseeing of managers and, thus, minimise conflicts of interest between agents and principals, so they could be seen as appealing to boards when viewed a theoretical perspective (in accordance with the Cadbury Committee, 1992).

Chen, Cheng, and Wang (2015) documented that board independence has resulted in improved financial reports; thus, it is commonly known as one of the most important elements when it comes to fulfilling shareholders’ interests. Furthermore, it has been maintained that independent directors can be defined as the individuals allocated with the task of representing shareholders and alleviating any conflicts of interest between them and managers (Fuzi, Halim, and Julizaerma, 2016, p. 460). Additionally, according to Zhang (2012), board independence is widely acknowledged as being a key player in offering shareholder data and alleviating firms’ negative reputations. Hence, in light of the fact that board independence is clearly a factor of much importance, a wealth of research centred on the relationship between firm performance and board independence has been conducted.

The existing literature within this area has, perhaps unsurprisingly, yielded somewhat variable outcomes. Some studies have concluded that there is a negative relationship between firm performance and foreign independent directors (Masulis, Wang, & Xie, 2012), while others (i.e., Abu-Tapanjeh, 2006; Baysinger & Butler, 1985; Brown & Caylor, 2004; Byrd & Hickman, 1992; Rosenstein & Wyatt, 1990) have documented the existence of a positive relationship between firm performance and board independence (and its aptitude in monitoring management). From the latter conclusion, we can surmise that some limits surrounding managerial discretion could be put in place with the aid of board independence. Identifying board independence as a notion of employees, principal owners, and the firm’s management, another investigation documented the existence of a positive relationship between Swedish firm performance and board independence (Palmberg, 2015). Conversely, in a study conducted
by Fuzi et al. (2016) a positive relationship was documented between firm performance (ROA) and board independence.

Possibly as a result of the notion that independent directors tend not to be given sufficient data concerning the firm, a wealth of research within this area has concluded that there is actually a negative relationship between firm performance and board independence, since NEDs do not possess the necessary skills here. Such a view would appear to lead to the conclusion that, as maintained by Franks, Mayer, and Renneboog (2001) and Agrawal and Knoeber (1996), independent directors are not in a position to head the monitoring of managers. One investigation in this field did, indeed, find there was a negative relationship between UK firm performance and board independence (Weir & Laing, 2000); however, it was actually as a result of the firm’s negative performance that independent directors suddenly became so commonly used, and, in turn, why their presence became linked with bad firm performance. Hence, it seems unlikely that this was a case of correlation rather than causation. On a similar note, while independent directors have become somewhat of a hot topic among debates for US and UK corporate governance, the studies conducted on this topic (e.g., Hermelin & Weisbach, 1991; Hossain, Prevost, & Rao, 2001; Mehran, 1995; Vafeas & Theodorou, 1998; Yermack, 1996) did not find any positive relationship between firm performance and board independence; nor did Bhagat and Black (2002), Klein (1998), and Agrawal and Knoeber (1996) find a negative relationship between these two factors.

Notably, it was detailed in a 2018 study that there was a positive relationship between the early paying off of debt (of course, with the aim of alleviating bankruptcy risks) and board independence (Meder, Schwartz, & Young, 2018). A similar study also concluded that there was a positive relationship between internal monitoring and board independence—a conclusion that ultimately validates agency theory and leads to the management of both short- and long-term debt maturity (Tosun & Senbet, 2020). Such results allow for a more detailed understanding of how mixed results could be garnered from studies as a result of a lack of acknowledgement of corporate governance mechanisms and their role as moderating factors.

To conclude this subsection, some of the research conducted concerning the relationship between firm performance and board independence within the context of the GCC region will now be examined. One such investigation documented a negative relationship between Oman firm performance and board independence (Al-Matari et al., 2014b), while in stark contrast, Alsartawi (2019) observed the existence of a positive relationship between Islamic bank performance (in terms of TQ and ROA) and board independence.
Board Outsiders and Firm Performance

The works of Xie, Davidson, and DaDalt (2003) and Klein (2002) have maintained that better financial reporting could be attained by implementing external board members, as this could result in an independent monitoring mechanism.

While the widely accepted definition of the term ‘outside directors’ in Kuwait is also that of independent directors, Johnson et al. (1996) define them as, ‘… all non-management members on the board’ (p. 417). However, as noted by Rediker and Seth (2005), the definition of ‘independent’ within this term varies for each nation; the Kuwaiti definition of this term refers to independence both from a major shareholder and from management. Notably, as investigated by the likes of Jiraporn et al. (2009), Peng (2004), Tihanyi et al. (2003), Johnson, Hoskisson, and Hitt (1993), and Pearce and Zahra (1992), possessing a large proportion of independent external directors is the topic of much research within this field, since the arrangement of such directors is an area requiring further clarification.

It has been maintained that, in order to guarantee outsiders success in controlling, firms require leadership from a good board. Furthermore, it is worth noting that a great deal of stress was placed on all Kuwaiti firms to allocate a specific ratio of independent directors to their board in 2013 in order to enhance their corporate governance. It has also been stated that after a rapid decrease in firm performance takes place, external directors are the most proficient in creating a disciplined restructuring programme (Perry & Shivdasani, 2005). Indeed, considering they have the ability to voice their own external opinion, implementing experienced external directors is likely to garner a wider, more comprehensive understanding of the business’s operations from an impartial perspective—despite the fact that executive or internal directors are, of course, essential to the successful running of a firm.

Notably, a study within this area concluded that there was a positive relationship between non-financial firm performance (ROA) and board outsiders (Pombo & Gutiérrez, 2011). Similarly, another body of research in this area concluded that there was a positive relationship between firm performance (particularly family-owned firms) and board outsiders through the lens of agency theory (Maseda, Iturralde, & Arosa, 2015).

Furthermore, Arosa, Iturralde, and Maseda (2010) stated that the role of either a steward or agent can be undertaken by outside directors, suggesting that firm performance was measured via the (independent and affiliated) outsiders’ traits. Notably, the conclusion of this study indicated a positive relationship between firm performance (particularly in family-owned
firms) and board outsiders. In the same vein, a similar study in 2016 concluded that there was a significant relationship between firm performance and board outsiders for the 92 studied UK insurance firms (Adams & Jiang, 2016).

It is worth noting that the research conducted in this area yielded largely variable results. This is evidenced by the fact that one such study documented the existence of a positive relationship between family-owned firm performance and board outsiders (Arosa et al., 2010), while another conducted one decade later outlined that a very clear positive relationship was identified between firm performance and board outsiders (Fernández & Tejerina, 2020).

While this particular investigation did possess omitted variable bias (which resulted in some varied and invalid findings), it is worth noting that another study conducted in 1985 documented the existence of a positive relationship between the 266 studied US firms’ performance and board outsiders (Baysinger & Butler, 1985). However, the reason for this bias and, thus, lack of validity, lies in the fact that the researchers did not control for any of the other factors that may have influenced firm performance, nor did they control for any of the contrail variables. Furthermore, the use of ROE as a tool further invalidates this particular study, since this tool is known for being particularly controlled by management.

Noting the existence of a positive relationship between UK firm performance (TQ) and a large number of board outsiders, Mura (2007) implemented the generalised method of moments (GMM) approach when conducting this research to account for any possibility of endogeneity, and also highlighted that UK firms have done a better job of monitoring managers since the introduction of the Cadbury Code. Similarly, a positive association between the 526 studied US firms’ performance (ROA) and board outsiders was documented in a 1989 study, although here no identifiable relationship was documented between ROE as proxy of firms’ performance and board outsiders (Schellenger, Wood, & Tashakori (1989). Finally, another study in 2007 concluded that the relationship between firm performance and board composition was an endogenous one (Dahya & McConnell, 2007). In spite of all of the clear, empirical results above, many would argue that this documentation of a positive relationship between firm performance and board outsiders is likely to be just an indicator of the correlation between the time at which these studies took place (i.e., one where firms were already typically performing well, regardless of board outsiders).

To continue with the studies in this area, a positive relationship between the 142 studied US firms’ performance and board outsiders (treated as endogenously determined) was documented
by Hermalin and Weisback (1991), although they also mentioned that they did not identify a clear relationship of any nature between these firms’ performance in terms of $TQ$ and board outsiders. Although this particular research did not control for other potentially influential variables, in a similar study it was concluded that there was no identifiable relationship between the 100 studied US firms’ performance and board outsiders (Zahra & Stanton, 1988). Furthermore, while neither of these studies controlled for any potentially confounding variables, it is worth noting that both Mehran (1995) and Yermack (1996) identified the existence of both a negative relationship between firm performance ($TQ$) and board outsiders and no significant identifiable relationship between firm performance ($ROA$) and board outsiders in US firms. The same inconclusive results were found when measuring the relationship between the 54 studied firms’ performance and board outsiders (Dulewicz & Herbert, 2004), while Agrawal and Knoeber (1996) identified the existence of a negative relationship between the 400 studied firms’ performance ($TQ$) and board outsiders. Notably, from these bodies of research, we are yet to find sufficient evidence to support the notion that firms that have board outsiders tend to be more lucrative than those that do not.

From all of the above, it can be concluded that the variable outcomes yielded from the above studies have possibly arisen as a result of the different regression models utilised, as well as the differences in corporate governance among the nations studied.

### 4.3.3 Audit Committee Characteristics and Firm Performance

According to Cadbury (1992), a widespread interest in audit committees has been attained due to their ability to deftly manage and improve a given firm’s financial management and to increase the amount of accountability maintained within a firm. Indeed, the likes of the Cadbury Report (1992) have maintained that the key role of audit committees is to endorse and protects shareholders’ interests. As pointed out by Badolato and Donelson (2014), a sufficient audit committee, through the lens of agency theory, will monitor managers, the process of financial reporting, and the internal controls of the firm. Furthermore, Weir et al. (2002) pointed out that the audit committee is largely acknowledged as a particularly pivotal internal governance mechanism when it comes to enhancing a given firm’s management of finances and, accordingly, the firm performance. In a similar vein, it is essential that any boundaries or stipulations that have been put in place can alleviate the firms themselves from being the entity at fault, since firms’ reporting quality, honesty, and corporate responsibility are the key traits audit committees are advised for (Zhang, Zhou, & Zhou, 2007). Saying this, it has been recognised that high anticipation for the positive influence audit committees will bring to
corporate governance (Rezaee, 2009) should be diminished where possible (Spira, 2007; Turley & Zaman, 2004). Nevertheless, it has been maintained that, regardless of whether it involves auditing or reporting, audit committees tend to alleviate moral- and selection-related agency issues (Rainsbury, Bradbury, & Cahan, 2008).

Allowing for the provision of shareholder safeguarding and accurate data to the public, the essentially implementing of audit committee largely arises from its capability to monitor both inside and outside auditors and direct firm managers, all with the ultimate aim of minimising any erroneous activity within the firm. Notably, Tanjung (2020), Al-Baidhani (2014), and Buchalter and Yokomoto (2003) have investigated this area, all drawing the conclusion that audit committees are among the most important elements of corporate governance when it comes to minimising monetary issues within firms. Such a notion is also expanded with the finding that firm performance and income can both be enhanced via audit committees’ inherent durability (Burke et al., 2019).

One such body of research concluded that there was a positive relationship between an audit committee’s characteristics and its success. The researchers reached such a conclusion as a result of their metanalysis of 103 of the other studies within the literature investigating the quantitative success of audit committees (Bedard & Gendron, 2010). On the other hand, another study documented that there was no identifiable relationship between firm performance (ROA) and audit committees, and firm performance and the structure of a given audit committee (Vafeas & Theodorou, 1998). Furthermore, both Beasley et al. (2009) and McDaniel, Martin, and Maines (2002) maintain that there was a positive relationship between firm performance and the utilisation of audit committees. Meanwhile, Raghunandan and Rama (2007) stated that conflicts of interest between principals and agents can be reduced by holding regular audit committee meetings, since this would signpost a meticulous audit committee.

Ultimately concluding that there was a positive relationship between in-firm honesty and the initiation of management training, another study within this area researched upwards of 355 firm audit executives in order to measure audit quality (Carcello et al., 2018).

Notably, agency theory stipulates that corporate governance can be enhanced by utilising an internal audit function. This was showcased within a study concluding that there was a positive relationship between improving the board of directors’ characteristics (board outsiders, board independence) and utilising internal audit functions, and a positive relationship between internal audit functions and audit committee characteristics, when studying the nature of the
link between corporate governance and the utilisation of internal audit functions (Eulerich, Kremin, & Wood, 2019).

Another example of research within this area would be that conducted in 2012, which outlines that a given firm’s aptitude for spotting erroneous financial behaviour can be increased by utilising a good internal audit function, since this facilitates the existence of a high-quality system for checking any accounting data (Sarens, Abdolmohammadi, & Lenz, 2012). Furthermore, another study observed that there was both a positive relationship between audit committee tenure and regular audit committee meetings and a negative relationship between the presence of auditing experts and an investment in internal auditors (Barua, Rama, & Sharma, 2010). Meanwhile, the topic of another study concerned the ways in which corporate governance could be enhanced by implementing internal audit valences on the grounds that a new internal audit function aided business managers’ performance (Danescu, Prozan, & Prozan (2015). Finally, the conclusion was drawn in 2015 that there is a positive relationship between firm reputation and the hiring of sufficient internal audit functions, since such hiring also leads to the hiring of an equally good quality external auditor (Zain, Zaman, & Mohamed, 2015). In light of all of the above, the subsection below centres on the existing studies investigating the relationship between firm performance and each of the individual characteristics of audit committees.

Audit Committee Size and Firm Performance

According to Vinten and Lee (1993), any given audit committee is required to possess a number of members that is sufficient for undertaking the tasks to ensure that committee’s success, three people being the minimum number required in Kuwaiti firms. Furthermore, as noted by Afza and Nazir (2014) and Pucheta and De (2007), a wealth of the current literature pinpoints that audit committee size is one of the elements that has most influence on ultimate firm performance. As may be expected, the conclusions drawn from each of these studies are rather varied, since many of the studies conducted within this area have been inconclusive. Regardless, much of the research also points out that there is a very clear positive relationship between firm performance and audit committee size. One such study in UK reached this conclusion after investigating the relationship between these two factors in non-financial firms (Zabojníková, 2016), while another conducted in the same year concluded that there was a positive relationship between Indian firm performance and audit committee size (Bansal & Sharma, 2016). Another set of researchers similarly stipulated that a large audit committee would bring stakeholders additional financial opportunities, perspectives, thoughts, and
skillsets (Saibaba & Ansari, 2012; Ujunwa, 2012). Such a notion was supported by Baxter and Cotter (2009), who concluded that when it comes to the extreme oversight of financial reporting within firms, large audit committees are better equipped to do this well, since they are more likely to possess individuals with a wide scope of skillsets to aid in such a matter.

Notably, a similar study documented the existence of a positive relationship between the profitability of Iranian firms and the size of their audit committees (Salehi, Tahervafaei, & Tarighi, 2018). Similarly, another set of researchers concluded that there was a positive relationship between the 50 studied Nigerian firms’ performance (ROA) and audit committee size (Orjinta & Evelyn, 2018). Meanwhile, another study observed the existence of a positive relationship between firm performance (TQ and ROA) and audit committee size (Al Ani & Mohammed, 2015), while another conducted in 2014 found the very same result (Ojeka, Iyoha, & Obighemi, 2014). Furthermore, it was maintained within another study that enhanced firm performance is certain to be attained with the implementation of frequent audit committee meetings, as this would lead to better oversight of managers (Raghunandan & Rama, 2007). Notably, a positive relationship between firm performance and a larger audit committee size was also documented by Alqatamin (2018). Since an audit committee possesses additional material dedicated to tackling any in-firm problems, it is seen as certain to be more successful when it is larger in size, according to resource-dependency theory. Similarly, Pearce and Zahra (1992) maintain that there is a consistently positive relationship between firm performance and audit committee size.

In stark contrast to the above, the likes of Menon and Williams (1994), Pincus, Rusbarsky, and Wong (1989), and Eichenseher and Shields (1985) documented the existence of a negative relationship between firm performance and audit committee size. This directly contradicts the aforementioned notion that a smaller audit committee size would lead to reduced scope of knowledge and diversity within the committee, although it should be kept in mind that much of the below research does not support that smaller audit committees allow for enhanced monitoring of managers. Dharmadasa, Gamage, and Herath (2014), Lin (2011), and Drakos and Bekiris (2010) all maintain that a wealth of the skillsets and knowledge of members of large audit committees will be wasted as a result of surplus socialising during decision-making and a lack of cooperation amongfellow members. In contrast, it has been pointed out that smaller audit committees tend to be less proficient in evaluating multiple areas for firm development and, thus, in making logical alterations in approach (Hambrick, Werder, & Zajac, 2008). Meanwhile, considering they acknowledge that large audit committees lack general
competence, other researchers maintain that there is, in fact, a negative relationship between firm performance and size of audit committee.

Conversely, some parts of the current literature offer inconclusive results. As an example Belkhir (2009a), stated that firm performance and audit committee size tend not to have a significant relationship. Similarly, it was concluded in another study that if the audit committee is too small or large, the relationship between this and firm performance will ultimately be nonexistent (Dalton et al., 1999).

When it comes to the research in this area conducted in the context of the GCC region, including Alzeban (2020) (Saudi Arabia), Al-Matari et al. (2014b) (Oman), and Al-Matari et al. (2012a) (Kuwait), the vast majority concluded that there was an overall positive relationship between firm performance (TQ, ROE, and ROA) and audit committee size.

**Audit Committee Meetings and Firm Performance**

Another audit committee characteristic that wields the potential to influence firm performance is audit committee meetings. When it comes to investigating the relationship between audit committee meetings and firm performance, one 2018 study conducted in the Malaysian context concluded that this relationship was a positive one (Wan Mohammad et al., 2018). Moreover, it has been claimed that one of the key roles of the audit committee is to offer empirical findings that indicate the positive relationship between internal audit advice and regular audit committee meetings, as well as to oversee and evaluate managerial feedback regarding any internal audit advice or findings (Alzeban & Sawan, 2015).

The intricacy of the way in which the firm runs, as well as the firm’s terms of reference, ultimately influence the total number of audit committee meetings arranged, despite the fact that it has been widely acknowledged that a minimum of three audit committee meetings should be held annually without any executive board members being present. Indeed, a wealth of studies, such as Collier and Gregory (1999), McMullen and Raghunandan (1996), and Menon and Williams (1994) have all quantified audit committee participation via the regularity of audit committee meetings.

As highlighted by McMullen and Raghunandan (1996), firms that do not encounter many monetary problems typically hold audit committee meetings far more regularly than those that do. So we can see that, as observed by Hoque et al. (2013), there is a significant positive relationship between firm performance and regular audit committee meetings. Indeed, this finding ultimately supports the notion that monitoring of managers and financial operations
within the firm can be improved via frequent audit committee meetings, as these usually cover the topic of preparing for and creating the firm’s financial report. According to McMullen and Raghunandan (1996), in order for the minimum of four audit committee meetings a year, as required by the Kuwait Code of Corporate Governance, to be totally effective, it is necessary to ensure that these meetings are frequent and well organised; this would help to promote management of the control system, general communication between members, and, in turn, firm performance as a whole. Furthermore, Vafeas (1999) maintains that sufficient internal control and monitoring of financial reporting can only be guaranteed through frequent audit committee meetings. Such a high level of organisation could potentially be promoted with a schedule, whereby internal deadlines are established in line with the publication of financial statements and the audit cycle.

Notably, the studies of Kyereboah (2008), Saleh, Iskandar, and Rahmat (2007), Abdul Rahman and Haneem (2006), and Xie et al. (2003) have all offered evidence to support the notion that the majority of the views surrounding the nature of the relationship between audit committee meetings and firm performance are very varied, although it has been noted fairly consistently that this relationship is always a significant one, regardless of whether it is positive or negative. A study within this area did, however, observe that there was a positive relationship between the 118 studied Australian firms’ performance ($ROE$ and $ROA$) and audit committee meetings, which also resulted in more trusted corporate governance mechanisms within Australian firms (Hoque et al., 2013).

Notably, regular audit committee meetings between both inside and outside auditors provide opportunities to evaluate the current audit procedure, the firm’s internal controls, and the firm’s current financial reports and are necessary for the committee to fulfill its role of monitoring risk management, the audit procedure, financial reports, and the internal accounting control, as well as to ensure that it provides annual and quarter-yearly financial statements. While the observations documented by researchers within this field are rather varied, both Saleh et al. (2007) and Abdul Rahman and Haneem (2006) concluded that there was a significant relationship between Malaysian firm performance and the regularity of audit committee meetings. Furthermore, both Kyereboah (2008) and Vafeas (1999) documented the existence of a positive relationship between firm performance and audit committee meetings as a result of these meetings’ impact on members. Notably, the former study (Kyereboah, 2008) noted that there was a positive relationship between firm performance ($TQ$) and audit committee meetings, but not when firm performance was measured by $ROA$—probably because the
population examined was Nigerian and South African. Furthermore, Alqatamin (2018), Ojeka et al. (2014), and Xie et al. (2003) all concluded that firm performance can be improved as the quality of earnings improves—something that can be achieved with audit committees that endeavour to enhance the honesty of their corporate earnings. It has been suggested that audit committees must be both active (i.e., participating in a wealth of meetings) and individual in order to be considered successful (Menon & Williams, 1994). The researchers who stated this did find there was a negative relationship between Ghanaian firm performance (ROA) and audit committee meetings (Menon & Williams, 1994). To offer a quantitative solution, a total of four meetings a year has been recommended by Rezaee, Olibe and Minmier (2003).

Notably, both Sharma, Naiker, and Lee (2009) and Rebeiz and Salameh (2006) concluded that there was no significant identifiable relationship between firm performance and audit committee meetings. Another study, however, documented the existence of a negative relationship between firm performance and slightly increased regularity of audit committee meetings, likely as a result of uncertainty in decision-making and the financial implications incurred by regular meetings (Evans, Evans, and Loh, 2002). The key roles of the audit committee include overseeing financial reporting and performance; how ‘active’ audit committees are deemed to be in fulfilling these roles is generally determined by the number of meetings held (Abdul Rahman & Haneem, 2006). Conversely, it could also be supposed that audit committees are more likely to better fulfill these roles when there are fewer meetings (Saleh et al., 2007), since less discretionary currency accruals are more abundant when there are fewer meetings (Xie et al., 2003).

Furthermore, mixed findings regarding the relationship between firm performance and audit committee meetings have been documented in all of the research conducted within the GCC region: while one concluded that there was no identifiable relationship between these two factors in Saudi Arabia (Al-Matari et al., 2012b; Alzeban, 2020), another documented the existence of a negative relationship between the two in the context of Oman (Al-Matari et al., 2014b).

**Audit Committee Independence and Firm Performance**

This particular paper surmises that there is a strong relationship between firm performance and audit committee independence, since issues regarding conflicts of interest are incurred without audit committee independence, which requires a good-quality audit committee to step in. Indeed, according to Abbott, Park, and Parker (2000) and Jensen and Meckling (1976), the audit committee is generally regarded as a subcommittee of the board of directors that
ultimately increases the effectiveness of corporate governance. Furthermore, as penned by Munro and Buckby (2008), when it comes to their task of monitoring managers, independent directors are not at risk of pursuing their own firm-related interests because they do not have any. In line with this, we can conclude that risk assessment can be enhanced through the use of such audit committee independence (Cohen & Hanno, 2000). Seventy-eight has been suggested as the most effective number of independent audit committees that one member should employ so as to improve the firm’s financial reporting (García & Sanchez, 2009)—the transparency of which, according to Bradbury (1990), independent audit committees are proficient in upholding.

Audit committee defined by Al-Matari et al. (2014a) as a monitoring mechanism that ensures effective correspondence between the internal monitoring system, the inside and outside auditors, and the board of directors, it has been suggested that a minimum of three NEDs should be assigned to the audit committee and chaired by independent members (Code of Kuwait Corporate Governance, 2013). Notably, Zhou, Owusu, and Maggina (2018), Farber (2005), and Dezoort and Salterio (2001) all maintain that in cases where paraphrasing of financial statements is deemed a failure, such paraphrasing may not be anticipated. Furthermore, when it comes to handling conflicts of interest between agents and principals, independent supporters can aid external auditors.

According to Mallin (2006), the key role of an audit committee is to monitor financial reporting and to safeguard shareholders’ interests, and this is an essential corporate governance mechanism. In a study conducted in 2013, it was concluded that there was a significant relationship between the 106 studied Amman financial firms’ performance and audit committee independence (Hamdan, Sarea, & Sameh, 2013), while another study in this area documented the existence of a positive relationship between firm performance ($TQ$) and audit committee independence. Furthermore, while another set of researchers observed a significant relationship between Ghanaian insurance firms’ performance and audit committee independence (Tornyeva & Wereko, 2012), Bouaziz and Triki (2012) similarly concluded that there was a significant relationship between the 26 studied Tunisian firms’ performance ($ROE$ and $ROA$) and audit committee independence.

In the same vein, a recent study documented the existence of a positive relationship between firm performance and audit committee independence (Schrader & Sun, 2019), while another concluded the same findings, which supported their own hypothesis (Perez, Quevedo, & Delgado, 2019). Similarly, it was observed in 2019 that there was a positive relationship
between firms’ compensation systems and audit committee independence (Schrader & Sun, 2019). This same result was also documented by Moses (2019) in the context of Nigeria.

In contrast, a study investigating the relationship between these two factors concluded that there was no significant identifiable relationship between the 20 studied Nigerian firms’ performance and audit committee independence (Kajola, 2008)—and, on top of this, no relationship between firm performance and the presence of NEDs was documented. While this finding does not support the notion that a positive relationship between these two audit committee independent and firm performance should always be anticipated, it does support the researchers’ results: that there was no significant identifiable relationship between firm performance and audit committee independence (Al-Matari et al., 2012b). Saying this, Al-Matari et al. (2012c) do maintain that agency problems can be alleviated via audit committees. Furthermore, the non-existence of a significant relationship between these two factors was additionally documented by Klein (1998). This result is supported by the findings of Ghabayen (2012), whose study was conducted in the Saudi Arabian context. Finally, when it comes to the GCC context, Al-Matari et al. (2014b) and Al-Matari et al. (2012b) confirmed that there was a positive but insignificant relationship between Omani and Saudi Arabian firms’ performance and audit committee independence.

**Audit Committee Expertise and Firm Performance**

Audit committee expertise is yet another component of an audit committee that has the potential to impact many elements of a given firm, and, in the USA, it is necessary for any given board to comprise more independent directors than any other member type, as well as at least one financial expert (Sarbanes Oxley Act, 2002). Choi, Han, and Lee (2014) concluded within their study that financial literacy is of high importance when it comes to mandatorily established audit committees and diverse firms. Furthermore, another study maintains that there is a positive relationship between firm performance and audit committee expertise because audit committee expertise often enhances the quality of the financial report (Baxter & Cotter, 2009). Hence, this study indicates that an audit committee with high experience in finance is essential. It was also documented in 2011 that investors find audit committees with expertise in finance appealing (Carcello, Hermanson, & Ye, 2011).

Attempting to cover the area that had been missed by previous researchers in the area, a study conducted in 2014 observed that there was a positive relationship between Malaysian firm performance (*ROE* and *ROA*) and internal audit committee expertise (Al-Matari et al., 2014a), with Hutchinson and Zain (2009) similarly concluding that there was a significant relationship
between the 60 studied Malaysian firms’ performance (ROA) and internal audit committee experience. Meanwhile, another instance of a positive relationship between firm performance and audit committee expertise in finances was documented (Davidson, Xie, & Xu, 2004)—a finding that was supported by the observations of Qin (2007). Meanwhile, another study concluded that there was a positive relationship between Palestinian firm performance and audit committee financial expertise (Musallam, 2020). Furthermore, in an attempt to explain their similar finding (i.e., that there was a positive relationship between firm performance and financial literacy in audit committees), El Mi and Seboui (2008) stated that this is likely due to the fact that strong governance is greatly encouraged with financial expertise when it comes to monitoring management, ensuring accounting rules and regulations are upheld, and increasing shareholders’ income.

The aforementioned consistent results indicating a positive relationship between audit committee expertise in finance and firm performance are explained through the notion that the overseeing of firms’ financial systems is made easier and more effective when audit committees are financially fluent (Xie et al., 2003). This claim is supported by McDaniel et al. (2002), who outlined that financial literacy in audit committees encourages a higher quality of financial reporting. Meanwhile, such justification is continued with the statement that since the audit committee shoulders the burden of the entire financial reporting process, it is essential that audit committees are financially competent and experienced (Schmidt & Wilkins, 2013). Similar to the aforementioned notion put forward by McDaniel et al. (2002), Defond, Hann, and Hu (2005) remind us that shareholders’ income will surely be increased with the strong corporate governance encouraged by experienced audit committees. Furthermore, Krishnan and Visvanathan (2008), Zhang et al. (2007), Saleh et al. (2007), and Krishnan (2005) all maintain that there is a strong positive relationship between the time-efficiency and quality of financial reporting and audit committee financial literacy.

In a meta-analysis of some 90 studies within the current literature, it was concluded that there is ultimately an undeniable positive relationship between firms’ financial reporting quality and audit committee expertise, despite the admittedly weak findings of some of the examined studies—a process that also led to the definition of an audit committee financial expert being condensed (Chen & Komal, 2018). Furthermore, a positive relationship between audit committee expertise and the 266 studied Chinese firms’ high-quality financial reporting was similarly observed in another study (Lo, Wong, & Firth, 2010). In contrast, a barely significant
relationship was documented between Indonesian firms’ financial reporting and audit committee expertise (Florencea & Susanto, 2019).

Finally, it is worth noting that McDaniel et al. (2002) claimed that, when it comes to the operation, importance, and responsibility of the audit committee of a given firm, financial literacy has the potential to add incredible value to the structure at hand—and it can also enhance monitoring of managers. Indeed, when all of the aforementioned studies are viewed side-by-side, it can be seen that the vast majority of them very clearly indicate that there is a positive relationship between firm performance and audit committee expertise—a result that may indicate an international mindfulness in terms of assigning the correct tasks to the correct people.

4.4 Chapter Summary

A detailed summary of some of the problems associated with firm performance and how this is impacted by faulty corporate governance has been provided within this chapter, in the context of both developed and developing nations. Indeed, a wealth of the literature within this area that we have examined has provided a deeper comprehension of the way in which corporate governance operates within a given firm and the impacts it wields on a wide range of business elements. The problems of audit committee characteristics, ownership structure, and board of directors’ characteristics have all been all discussed in relation to corporate governance and its overall impact and firm performance proxies, such as $TQ$, $ROE$, and $ROA$. Our aim to provide a comprehensive review of this topic for both developed and developing nations ultimately formed the foundation for the works examined and the results garnered.
Chapter 5: Ownership Structure, Corporate Governance Reform, and Firm Performance: Evidence from Kuwait

This chapter comprises a paper prepared as a working paper and submitted for publication in a peer-reviewed journal as follows:


This paper examines the link between ownership structure and firm performance in Kuwaiti industrial and services sector firms over the period 2010–2017 in the regulatory context of recent and extensive corporate governance code reform. Ownership structure is specified according to family, government, and local and foreign institutional investor ownership, and firm performance using the return on assets (ROA), return on equity (ROE) and Tobin’s Q (TQ). All measures of firm performance were found to positively relate to family, local institutional, and government ownership, accounting for anywhere between 12 and 28 percent of the variation in firm performance. Control variables in the form of firm size, debt-to-equity, leverage, and cash flow also displayed significant relations with firm performance. However, new, albeit thus far short-lived, corporate governance reforms appeared to have had little effect to date on firm performance in moving to a first voluntary then compulsory corporate governance code and guidelines.

STATEMENT OF CONTRIBUTION TO COAUTHORED PAPER

- The candidate’s contribution to this paper consisted of researching and writing the literature review, formulating and conducting the methodology, analysing and writing up the results, and preparing and formatting the text, tables, and figures.
- Andrew Worthington’s contribution to the paper involved guiding the research design and editing.
5.1 Introduction

Ownership structure is essential when it comes to understanding firm decision-making and its relation to earnings management, audit quality, and firm performance; indeed, a large number of studies consider the impact of various factors on good corporate governance processes and practices (e.g., culture, the level of development, and legal and political circumstances) (Hanafi, Setiyono, & Sanjaya, 2018). Notably, these are significant concerns given the fundamental need for firms to attract investment capital, enhance corporate performance, and reduce investor risk. Furthermore, it is widely recognised that the structure of ownership or who owns the firm (as distinct from the legal type of ownership, whether sole proprietorship, partnership, or private and public firms) strongly influences firm performance in the operation of global firms.

Ownership structure in this sense relates to the mix of large and small, individual and institutional, local and foreign, and private and public sector shareholders, among others, the expectation here being that particular ownership structures are able to improve firm performance, regardless of measurement methods, through sound management and the well-considered allocation of firm resources. On this note, some types of ownership arguably improve professional conduct in business and, accordingly, limit the opportunities for risk, fraud, or embezzlement (Naimah, 2017; Palmberg, 2015), while others widen the network of business contacts; meanwhile, others bring business expertise for the firm’s implementation. All encompass corporate governance, since this is the framework that defines the relationship between shareholders, management, and the board of directors, and the way in which it influences how a firm operates and performs.

While there is, indeed, abundant research on many of these issues within the well-developed markets and regulatory regimes found in advanced economies, such research is lacking in nearly all developing economies (Rahman, Ibrahim, & Ahmad, 2017)—something that is important since the marginal gains to good governance (which flow from the ownership structure and the regulation within which it operates) are much larger within such economies, and thereby have the potential to be more influential in improving firm and economic performance and, with them, shareholder and stakeholder wellbeing.

Family ownership can be defined as a firm that is owned either wholly or majorly by two or more related parties with or without a management role or board representation, and is one of the more common types of ownership—particularly in developing countries (Yang, 2010). Indeed, this is especially the case in Kuwait, since here, the royal family

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(the House of Al-Sabah) is a major shareholder in several firms. As stated by Jensen and Meckling (1976), the agency problem, which is incurred as a result of the mixing of control and ownership that facilitates shareholders to trade private rents and profits, is a very frequently encountered hurdle within family ownership. Indeed, family-owned firms are generally regarded as not lucrative or reliable by traditional studies in this area, often centring on the negative aspects of family firms. The basic argument is that family ownership is associated with improved firm performance, one dimension of this being that family members have access to more and better internal information and can thus better foresee the performance prospects of a given firm—something that, in turn, allows them to make better decisions regarding whether to reduce or increase their holdings. Another argument is that family members with a large share of ownership and both direct and indirect involvement in management help to resolve agency problems that otherwise continue to exist within more widely held firms. Saying this, the agency problem could be increased between family owners and minority shareholders. Furthermore, reduced agency costs were documented in well-monitored family-owned firms (Fama & Jensen, 1983a)—a positive result considering family firms were documented as being the most common type of firm across 27 different countries (La Porta et al., 1999).

In this study, the focus centres on the assessment of the relationship between ownership structure, regulatory reform, and firm performance within Kuwait—a small but influential country located in the Arabian Gulf. In recent years, the Kuwaiti Government has actively sought to attract local and international investors, as well as to encourage improved monitoring by shareholders. Furthermore, Kuwait’s Ministry of Commerce, as well as the Kuwait Stock Exchange (KSA), have also taken steps to improve corporate governance within its largest (mostly listed) firms (Alfaraih et al., 2012). Ultimately, an improved understanding of ownership structure and its impact on Kuwaiti firm performance is an essential contribution to the overall goal of assessing the developments that have taken place, as well as those awaiting attention. Indeed, this should yield useful insights for the many dozens of comparable economies at similar stages of financial and economic development.

The structure this paper is as follows: Section 5.2 reviews the governance framework in Kuwait, with particular attention to recent regulatory reforms, followed by Section 5.3, which presents the tested hypotheses and discusses the related literature. From there,
Section 5.4 details the empirical methodology, while Section 5.5 discusses the results. Finally, Section 5.6 provides the conclusion for the chapter.

5.2 Corporate Governance Reform in Kuwait

When it comes to the link between a given firm’s performance and corporate governance, Kuwait differs greatly from its counterparts, although it is not the only novel market introduced within the GCC. This individuality is the result of several factors: firstly, corporate governance improvements, permitting economic and financial collaboration on a global scale, an increase in stock market interaction, and management in economic progression and amending, which have all been witnessed as a result of businesses within Kuwait recently undergoing large-scale changes in terms of deregulation within its markets and its privatisation. Furthermore, as could be seen in its role in the Gulf War in the late 20th century and its recovery after the Middle Eastern revolutions in the early 21st century, Kuwait’s economic progression has been largely furthered by the enhancements made to its fellow emerging markets (Abdallah & Ismail, 2017).

Another factor that differentiates Kuwait from the vast majority of developed countries is the simplicity of its tax system, since here, there are no corporate or personal taxes. This makes Kuwait a solid foundation for assessing corporate finance theory. Finally, Kuwait boasts royalty and a wealth of family ownership—something that most certainly sets it apart from its Middle Eastern counterparts.

Despite all of the above, it took until 2013 for Kuwait to incorporate its own general corporate governance policies and recommendations—something that was common practice in the majority of the Gulf countries by that point, having been adopted in 2002 by some. This led to Kuwait ranking behind most of its competitors when it came to the legislation underpinning its corporate governance, despite its amendments in 2016 to bridge any gaps and its introduction of a capital market authority in 2010. Furthermore, while the UAE and Bahrain possessed categorised policies for all state-owned firms, small and medium-sized enterprises (SMEs), bank and insurance organisations, and real estate agents, Kuwait only did this for banks—and, to add to this, Kuwait does not incorporate the comply-or-explain provisions within its policies, while Bahrain, Oman, Saudi Arabia, and the UAE do.

Such guidelines placing all the listed businesses under the obligation of amending their underpinning rules and regulations, any organisations listed on the KSA have to abide by
the 2016 company law and the 2010 Capital Markets Authority laws. The former is not investigated any further here, and both include the necessary distance between the CEO and chairman of the board, restrictions concerning loyalty to other boards (particularly competitors), a minimum number of board members, and the membership of independent directors. In addition to these things, the eradication of board members’, their families’, and managers’ trading deals without the go-ahead of fellow shareholders, as well as stringent guidelines surrounding the distributing of private data, are also outlined (Bouresli & Aldeehani, 2017).

In the same vein, the suggestion of such guidelines was done by the Capital Market Authority (CMA), all of the above being predicted to wield a positive influence on Kuwaiti firm performance due to the resulting improvements in overall corporate governance. Here, according to the timeline, compliance to policies was only required post-2016, before which compliance was voluntary for two years (2013–2015), and there was a complete absence of any policies before this time. In accordance with such a timeline, it is our aim to establish whether these transitions (from voluntary to compulsory compliance) have impacted firm performance in any capacity—and, more specifically, whether it has led to improvements.

### 5.3 Literature Review and Hypothesis Development

As stated by Abdullah and Valentine (2009) and Larcker, Richardson, and Tuna (2004), the entire notion of corporate governance has not been backed by any correlations, nor does it have any supporting research. Saying this, it is a valid aspect of global firm performance, and the likes of institutional theory (Suchman, 1995), stakeholders’ theory (Freeman, 1984), resource-dependency theory (Pfeffer & Salancik, 1978), stewardship theory (Donaldson & Davis, 1989), and agency theory (Jensen & Meckling, 1976) have somewhat taken steps towards supporting corporate governance. The existence of such an abundance of theories suggests that a combination of the best parts of each theory would facilitate the garnering of a well-rounded understanding of corporate governance, as was adopted by George (2005) and Eisenhardt (1989).

Agency theory and the conflicts it brings is an important consideration concerning ownership, and here, since it covers the relation between the firm’s principals (owners) and their agents (senior executives and managers), good corporate governance might be a possible solution (Shleifer & Vishny, 1997). Indeed, the majority of the existing
research in this area concludes that strong corporate governance helps manage the relationships and minimise the agency costs incurred by the separation of ownership and control (e.g., Hu & Izumida, 2009; Shleifer & Vishny, 1997). Different types of ownership (i.e., public vs. private, family vs. non-family, institutional vs. non-institutional, domestic vs. foreign) differ in their ability to manage these relationships in the interests of firm performance (Abdallah & Ismail, 2017; Romano & Guerrini, 2014) with overall corporate governance.

A wealth of research within this area has showcased the fact that when it comes to the operation of firms, ownership structure is essential. Within one such study, it was stated that there is concentrated corporate ownership within the majority of countries outside of the USA and UK (Zhuang, 1999); furthermore, the extent to which ownership structure impacts shareholders’ influence over a given firm was showcased by Tricker and Tricker (2015), who documented that since public firms’ ownership structures (no matter the country in which they are located) tend to be rather intricate, it is paramount that in order to understand the given firm’s authority and influence, we first understand its ownership structure.

Moreover, while one study found there to be a significant positive relationship between future firm performance and large shareholders (Zeckhauser & Pound, 1990), another two similarly concluded there to be a positive relationship between firm performance and ownership concentration (Kobeissi & Sun, 2010; Zeitun & Gang, 2007). Furthermore, another also documented the existence of a positive relationship between firm performance and managerial equity ownership (Mehran, 1995). Arouri et al. (2014), however, documented that while a positive relationship could not be found between firm performance and government ownership, one could be found between firm performance and foreign, family, and institutional ownership within Gulf Cooperation Council (GCC) banks. Meanwhile, among the studies in this field documenting a negative relationship between firm performance and ownership concentration was that of La Porta et al. (1999), who found that not transferring profits and not paying dividends to the firms that they exert authority over could lead to minority shareholders’ expropriation when shareholders are in charge of a given firm. Finally, an inconclusive relationship between firm performance and insider ownership was identified within a study by Morck et al. (1988).

It has been documented that there is a positive relationship between firm share prices and large shareholders (Shleifer & Vishny, 1997), despite the fact that both La Porta et al.
(1999) and Shleifer and Vishny (1997) suggested that a mismatch between non-controlling shareholders’ and shareholders’ incentives could lead to more harm than good, thus suggesting there to be a negative relationship between firm performance and large shareholders. Therefore, this study discussed family ownership, instutitonal ownership and government ownership, whereas these three types the only three common types in KSE.

5.3.1 Family Ownership and Firm Performance

As founded by Anderson and Reeb (2003), Faccio and Lang (2002), and Claessens et al. (2000), the vast majority of global firms’ capital stake largely comprises family ownership. Being a subject that has been widely debated among researchers within the field (a wealth of theories have also been developed in this respect), family ownership has been hypothesised to have the potential to cast a significant and direct impact on firm performance—although some do theorise that a negative impact is more likely to arise as a result of the implementation of family ownership. Regardless, the likes of Baydoun et al. (2013), Gadhoum, Lang, and Young (2005), Anderson and Reeb (2003), Faccio and Lang (2002), Franks and Mayer (2001), Claessens et al. (2000), and La Porta et al. (1999) all confirm within their respective studies that family ownership is very commonly implemented globally, including in Western European countries, Arabian countries, the USA, and Eastern European countries.

As maintained by Villalonga and Amit (2006) and Jensen and Meckling (1976), agency theory takes the perspective that family ownership is likely to reduce conflicts of interest between managers and owners (i.e., the agency problem). Such a notion is supported by Lee (2006) and Miller and Le (2006), who point out that firm performance is likely to be enhanced with family ownership due to the fact that family owners have more motivation to prioritise income and, thus, oversee their managers than those of other ownership structures. This is further supported by Shleifer and Vishny (1997) and Pollak (1985), who maintain that family business owners have more inherent drive to increase the business’s income. Alternatively, we could say that family ownership is more likely to emphasise the agency problem, according to Villalonga and Amit (2006), Fan and Wong (2002), and Fama and Jensen (1983b), since—as articulated by Corbetta and Salvato (2004)—family business owners may be more interested in fulfilling their own personal needs through their business, in turn undermining minority shareholders’ requirements.

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Meanwhile, Donaldson’s (1990) stewardship theory takes the stance that firm performance and family ownership are likely to possess a positive relationship, since family owners are incentivised to maximise firm performance and support other team members in doing so. This is furthered by the fact that, according to McVey and Draho (2005) and James (1999), family-owned firms tend to be very intentional when choosing their sources of investment, usually adhering to specific criteria in the process. Furthermore, according to Arregle et al. (2007) and Lee (2006), family owners tend to view their firm as something of value that can be passed on through generations, and, thus, they are more motivated than other owners to ensure the business’s survival. Furthermore, in light of this, it has also been concluded that family business owners tend to focus more on long-term goals and visions than that which is gratifying in the short term. Finally, according to Martikainen, Nikkinen, and Vähämäa (2009) and Wang (2006), family-owned firms are likely to see better-quality profit and additional income compared to businesses implementing alternative ownership structures, as family-owned firms tend to be governed by those who are motivated to keep the firm running, in turn allowing for more employee skillsets and knowledge with time.

Stating, according to Habbershon, Williams, and MacMillan (2003), that family-owned businesses inherently possess abilities and materials that automatically enhance firm performance, resource-dependency theory maintains that there is a positive relationship between firm performance and family ownership. This notion particularly seems to have merit when considering the fact that family-owned businesses have the potential to possess human, survivability, financial, and social capital, as well as trust and reputation, integrity and relationship commitment, and entrepreneurship (Aronoff & Ward, 1995; Arregle et al., 2007; Gibb, 2006; Horton, 1986; Lyman, 1991; Sirmon & Hitt, 2003; Zahra, 2003), all contributing to good firm performance.

It has been consistently found that family-owned businesses can, however, frequently engage in opportunistic behaviour that ultimately undermines shareholders, with Gomez et al. (2001), Morck et al. (2000), and DeAngelo and DeAngelo (2000) ultimately claiming that firms with managers that are large and unvaried, as is often the case with family-owned businesses, tend to be triumphed by firms with a more diverse team. This is backed by Carney’s (1998) notion that families tend to only allocate family members to top positions, and thus prioritise such familial matters over how qualified or able that person may be. This is similar to Shleifer and Vishny’s (1997) finding that family
shareholders have a habit of treating their business as a place for family to be employed, regardless of experience. Furthermore, Demsetz (1983) noted that family members often take limited materials from the business in order to fulfil their non-monetary recompense. Saying this, according to Miller and Le (2006), stewardship theory, in stark contrast to agency theory, is based on the assumption that individual behaviours are prefaced by varying psychological and environmental factors. Indeed, as pointed out by Jaskiewicz and Klein (2007) and Lane et al. (2006), stewardship theory has a high amount of application to family-owned businesses, since here, familial values tend to be placed higher than the experience of team members. Indeed, agency theory’s trademark selfish and opportunistiic behaviour is clearly less constructive than stewardship theory’s collectivistic and altogether more fruitful behaviour. In line with this, as documented by Pieper et al. (2008) and Davis et al. (1997), since stewards are typically more inclined towards pro-firm behaviours and decisions, there tends not to be a mismatch of interests between managers and owners within family-owned businesses, meaning an agency theory perspective may not be massively applicable here. Indeed, a wealth of research within the area conclude that family-owned businesses generally perform better than their non-family-owned counterparts. An example of this would be one conducted in 1998, which concluded that family-owned businesses possess higher stock market returns and market-to-equity ratios than similar non-family-owned businesses (McConaughy et al., 1998), while another similarly documented that family-owned firms in the S&P triumph over non-family-owned firms in terms of ROE and ROA by 6.65%, as well as in market value by 10% (Anderson & Reeb, 2003). Meanwhile, it has also been concluded that family-owned firms tend to run better with just family members as employees in cases where the firms’ legal protection is subpar (Burkart et al., 2003).

In spite of all of the above theories and research, the final conclusion regarding the nature of the relationship between firm performance and family ownership remains mixed—although some researchers (i.e., Anderson & Reeb, 2003; Martikainen et al., 2009; Villalonga & Amit, 2006) still conclude from their respective studies that the relationship between firm performance and family ownership is positive, particularly in developed countries. Martikainen et al. (2009) in particular surmised that there is a strong correlation between family-owned firm performance and the family’s previous wealth, since a high amount of wealth encourages long-term investment and efficiency.
Indeed, a positive relationship between firm performance and family ownership has consistently been found in studies conducted in Europe and Asia. One such study documented the existence of a positive relationship between the 435 studied firms’ market value and family ownership concentration after capital structure, nation impacts, and industry were all controlled for (Thomsen & Pedersen, 2000); similarly, another study concluded that there is a positive relationship between overall income-to-sales and ROA and family ownership (Yammeesri & Lodh, 2004). Meanwhile, another study, while concluding there to be a positive relationship between the founder being the CEO and firm performance, also found there to be a negative relationship between the descendants of the founder being the CEO and firm performance, since opportunistic behaviour increased as a result of their having less experience and motivation than the founder (Villalonga & Amit, 2006). Meanwhile, due to the fact that the managerial positions are undertaken by family members, a positive relationship between firm performance and family ownership was also documented by Nowak, Ehrhardt, and Weber (2006). In contrast, Palmberg (2015) and Al-Saidi (2013) documented there to be no significant identifiable relationship between firm performance and family ownership.

It has been consistently found that in Kuwait, and GCC countries in general, families who own their own firms tend to be highly concerned with the reputation of their firm and how this reflects on their firm, which encourages them to act in the best interests of the firm. Indeed, such a notion was backed by yet another study that noted the existence of a clear positive relationship between firm performance and family ownership (Arouri et al., 2014). Hence, in light of this, the following hypothesis was formulated:

**H1: There is a positive relationship between the level of family ownership and firm performance (ROA, ROE, and TQ) in Kuwaiti firms.**

### 5.3.2 Institutional Ownership and Firm Performance

Institutional ownership, which can be further partitioned into local and foreign institutional ownership, is another type of ownership with the potential to noticeably impact firm performance. Prior studies documented that the shareholders have different motivations according to agency theory; therefore, this study used local and foreign institutional ownership to see their impact on firm performance in Kuwaiti firms (Abdulsamad & Yusoff, 2016; Suhardjanto et al., 2017). As has been pointed out by Suddaby (2010), institutional ownership has become one of the most commonly known and researched types of ownership when it comes to evaluating firm performance, and
this is likely because, as stated by Zucker (1987), it allows for a more detailed understanding of firms. Institutional ownership is based on the premise that firm performance is positively impacted by institutional ownership shares growing in correspondence with the growth of investor expertise. Saying this, as pointed out by Young et al. (2008), Singh et al. (2005), and Gugler et al. (2003), varying structures of capital market and unstable institutions may mean that the rules and regulations made for developed markets may not be suitable for emerging markets, and so the utilisation of agency theory within such markets may prove to be redundant. Nevertheless, as stated by Filatotchev et al. (2013), it is essential that we garner a well-rounded understanding of such markets in order to understand corporate governance systems as a whole.

Furthermore, domestically accessible ownership is often seen to be triumphed by foreign institutional ownership in terms of garnered business contacts and overall firm performance. Indeed, it was noted in a fairly recent study that in-firm evaluation could be enhanced with the use of foreign institutional ownership in their corporate governance operations, since controlling shareholders are then less able to behave opportunistically (Huang & Zhu 2015). However, one study in this area notably concluded there to be a negative relationship between firm profit and institutional ownership, especially straight after they had broadcast bad news, as well as a tendency for firms to be less tenacious with accounting documentation (Lin, 2016); however, another two studies concluded there to be a positive relationship between governance structure quality and institutional ownership (Chung & Zhang, 2011; Schmidt & Fahlenbrach, 2017). Meanwhile, a study conducted in 2010 found there to be a positive relationship between employee motivations, firm monitoring, and firm performance and institutional ownership, especially with foreign institutional ownership (Elyasiani & Jia, 2010).

Similarly, the relationship between firm capital structure and institutional ownership has been the subject of a number of studies within this field. One conducted in 2014 documented the existence of a positive relationship between firm performance and internalisation and institutional ownership (Chen, Hsu, & Chang, 2014). Similarly, another related study found there to be a positive relationship between firm performance and institutional ownership because it encouraged more diligent firm monitoring (Chung & Wang, 2014).

As noted by Khanna and Palepu (2000) and Sarkar and Sarkar (2000), considering that the advantages that come with labour, technology, and capital can be undermined by
domestic ownership, foreign institutional ownership often triumphs over it. Indeed, as stated by Douma et al. (2006), foreign (and especially institutional) ownership has been consistently found to greatly impact firm performance, especially if such firms participate in the same areas, because then they will possess more expertise. Furthermore, as stated by Djankov and Hoekman (2000), foreign institutional ownership is typically associated with the swapping of explicit knowledge that usually cannot be shared, as well as that of more generalised knowledge (e.g., management skills, quality systems). However, there is, of course, much more to foreign institutional ownership than just these aspects.

Notably, a few studies in this area were, indeed, conducted in the GCC context. One study, concluding there to be no significant identifiable relationship between large institutional shareholders and Kuwaiti firm performance (Al-Saidi & Al-Shammari, 2015), ultimately garnered a very different result from our study, which may result from different types of institutional ownership (i.e., local and foreign) being at play, as well as different time periods. Nevertheless, another related study concluded there to be a positive relationship between the 58 studied banks’ performance and institutional ownership (Arouri et al., 2014).

Because, according to Maury (2006), their increased authority when it comes to voting leads to better decision-making and, in turn, firm performance (especially for businesses in the financial sector), institutional shareholding, according to Ehikioya (2009), Shleifer and Vishny (1997), and Kaplan and Minton (1994), has the potential to reduce the agency problem for firms that have investors as a result of their abundant knowledge and materials. Indeed, according to Denis and McConnell (2003), Claessens et al. (2000), La Porta et al. (1999), Shleifer and Vishny (1997), and Demsetz and Lehn (1985), a combination of large shareholders and institutional ownership is generally considered to be a key solution for the agency problem because their best interests lie in their best interests lie in closely monitoring enhanced firm performance. A wealth of research, including that by Mertzanis, Basuony, and Mohamed (2019), Suhardjanto et al. (2017), Balagobei and Velnamp (2017), Abdulsamad and Yusoff, (2016), Arora and Sharma (2016), Chen et al. (2014), Gurbuz and Aybars (2010), Omran, Bolbol, and Fatheldin (2008), Del and Hawkins (1999), and Chhibber and Majumdar (1999), has documented the existence of a positive relationship between firm performance and institutional ownership (both foreign and local)—which is somewhat unsurprising when considering
the fact that such ownership uses additional monitoring tools and processes. In light of this, the following hypotheses were formulated:

**H2**: There is a positive relationship between foreign institutional ownership and firm performance (ROA, ROE, and TQ) in Kuwaiti firms.

**H3**: There is a positive relationship between local institutional ownership and firm performance (ROA, ROE, and TQ) in Kuwaiti firms.

### 5.3.3 Government (State) Ownership and Firm Performance

According to Laidroo (2009), both in-firm decision-making and a given firm’s corporate governance are particularly impacted by government ownership—particularly in developing markets, where investment is key and firms tend not to fully privatise themselves. Since government-owned firms are obliged to share an abundance of information concerning the goings-on of their corporate governance mechanisms, it is likely that such firms will experience agency problems; this is even further exacerbated by the fact that it seems probable that any given government will have both profit-related and non-profit-related objectives, and thus will not place shareholders’ needs at the forefront of their decisions (Eng & Mak, 2003), political matters tending to be what motivates them the most. Furthermore, it has also been supposed that government-owned firms will likely implement subpar corporate governance operations, since accountability and monitoring tend not to be these firms’ strong points (Mak & Li, 2001). Finally, considering the fact that the government is effectively in charge of all stakeholders, it is likely that the government will insist on the firms they own sharing more information concerning their stakeholders than is usual (Ghazali & Weetman, 2006).

Conversely, it has been suggested that government-owned firms may be more likely to perform well than their family-owned counterparts, since, according to Shleifer and Vishny (1994), such firms would have government officials as their close contacts, as well as politically influential individuals. Such a notion is supported by the claim that government-owned firms will also be more incentivised to control and monitor the firm more diligently as a result of the large amount of shares the government has (Saal & Parker, 2000), thus leading to higher income and reduced agency problems. Furthermore, despite the fact that there is the issue of share prices massively dropping during times of financial peril (since this minimises shareholder losses) in such government-owned
businesses, Eng and Mak (2003) point out that government-owned businesses tend to see less asymmetric information.

Whether a minority or controlling interest is at play highly influences the extent to which government ownership impacts firm performance, as has been documented by the abundance of research conducted within this area. Meanwhile, the likes of Pan et al. (2014) document government ownership’s facilitation of monetary matters and such businesses’ abilities to circumvent administrative tasks. However, as documented by a study concluding there to be a negative relationship between firm performance and government ownership (especially within countries adopting civil law) (Borisova et al., 2012), it has been consistently found that low firm performance tends to be the catalyst for sudden government investment because it has a responsibility to help out the nation’s businesses during times of peril. Meanwhile, other studies, such as that by Ting and Lean (2015), document there to be no significant identifiable relationship between firm performance and government ownership.

Regardless of the results garnered, it is impossible to deny that the nature of the relationship between firm performance and government ownership has been a massive topic of research in recent years. While the likes of Alfaraih et al. (2012), Zeitun (2009), and Chen et al. (2005) have found very varied results concerning the nature of this relationship, a positive relationship between these two factors for firms in the United Arab Emirates (UAE), Malaysia, Singapore, and Kuwait has been documented by the likes of Alfaraih et al. (2012), Aljifri and Moustafa (2007), Ang and Ding (2006), and Najid and Rahman (2011). Meanwhile, the likes of Mrad and Hallara (2012), Liao and Young (2012), and Jiang, Laurenceson, and Tang (2008) also documented there to be a positive relationship between these two factors. According to Aljifri and Moustafa (2007), productive decision-making by management may be encouraged within government-owned firms, since there is less pressure to adhere to financial reporting rules and regulations here. Furthermore, it was also stated that government-owned firms may find their desired resources to be more easily accessible, since such firms tend to possess less asymmetric information (Eng and Mak, 2003). Finally, another study concluded there to be a positive relationship between the 514 studied Chinese firms’ performance and government ownership (Liao and Young, 2012).

Meanwhile, a wealth of research within this area, including that by Megginson and Netter (2001), Mak and Li (2001), and Xu and Wang (1999), concludes there to be a negative
relationship between firm performance and government ownership—and, indeed, a wealth of these studies have advised that whether the relationship here is positive or negative largely depends on the geographical location of the studied firms. Nonetheless, one study concluding there to be a negative relationship between these two factors stated that government-owned firms tend not to monitor or account for their operations sufficiently and are generally less able when it comes to adopting effective corporate governance mechanisms (Mak & Li, 2001). These findings, however, are problematic in the sense that they generalise the negative relationship between these two factors. Megginson and Netter (2001), Mak and Li (2001), and Xu and Wang (1999) also concluded there to be a negative relationship between the studied Singaporean firms’ performance and government ownership, justifying this finding by stating that government incentives usually lie in political matters and society as a whole, rather than in increasing firm income. Another study conducted in the context of the European Union (EU) similarly concluded there to be a negative relationship between firm performance and government ownership (especially in countries implementing civil law) (Borisova et al., 2012), and a negative relationship between Chinese firms’ performance and government ownership has also been documented by Xu and Wang (1999). Furthermore, a study conducted in the Jordanian context similarly documented there to be a negative relationship between the 59 studied firms’ performance and government ownership (Zeitun & Gang, 2007)—a finding that should likely be taken with a pinch of salt, considering the findings were likely not as straightforward as simply being negative. Despite all of the above, a wealth of other research, including that by Demsetz and Villalonga (2001), Demsetz and Lehn (1985), and Demsetz (1983) have documented there to be no significant identifiable relationship between firm performance and the adopted ownership structure.

Since the Kuwaiti Government is extremely honest with its corporate governance mechanisms and constantly backs any new laws or regulations that guarantee the safeguarding of financial market investors, overall, a positive relationship between Kuwaiti firm performance and government ownership is anticipated. In light of this, the below hypothesis was formulated:

\[ H4: \text{There is a positive relationship between government (state) ownership and firm performance (ROA, ROE, and TQ) in Kuwaiti firms.} \]
5.4 Method

The sample for this study comprised Kuwaiti industrial and services firms listed in the KSE over the period 2010–2017. Notably, there are, in the view of the KSE, eight variations of business involved in the industrial and services sector, encompassing a total of 682 firm-years (see Table 5.2). Considering the fact that, according to Mehran, Morrison, and Shapiro (2011) and Alsaeed (2006), such firms possess specialised rules and accounting practices and thus have the potential to mislead the results, firms within the financial sector were not included in this sample. Therefore, an unbalanced panel was used, the full sample comprising 682 firm-years. In this regard, two managers within the Kuwait stock market stated that:

The number of companies to have withdrawn from the national stock exchange, known as Boursa Kuwait, ‘skyrocketed’ in 2017, with 20 pull-outs occurring that year. The Chairman of Kuwait Industries Company Holding Mohammad Al-Naqi attributed the withdrawals to the companies’ ‘failure to meet stock exchange listing requirements’, in addition to diminished profits and a poor solvency ratio. (Kuwait Times, 2018).

Salah Al-Sultan, an advisor at Arzaq Capital Holding, cited certain provisos levied by Kuwait’s Capital Market Authority (CMA) as amongst the ‘chief reasons’ for the company pull-outs, besides geopolitical tension that has affected the stock market. (Kuwait Times, 2018)

Drawing on the discussion of the corporate governance reform in Kuwait and the missing values of some firms, the sample period (2010–2017) involved 520 firm-year observations as a net sample, our sample then being further partitioned into three subsamples corresponding to the three separate corporate governance code regimes. These were a pre-corporate governance code regime (2010–2012) and a voluntary corporate governance code regime (2013–2015), both with 390 firm-year observations, as well as a compulsory corporate governance code regime (2016–2017) with 130 firm-year observations. For the regression model, dummy variables were created for each regime, which took a value of one for the regime identified, it otherwise was zero.

Table 5.1 provides the descriptive statistics for the firms in this sector, including the number of firms, market capitalisation, capital value, traded value, and the number of outstanding shares. Meanwhile, Table 5.2 provides additional details on the industries in which these firms operate: as can be seen, the number of industrial and service firms listed
on the KSE has remained stable over the seven-year sample period, with the possible exception of a significant decline in the number of firms in 2017. This largely relates to the now-compulsory provision of the new corporate governance code; for example, prior to 2016, Kuwaiti firms were able to pledge their own shares in order to obtain funding, and the reforms removed this opportunity, thereby making financing more difficult. In addition, the new corporate governance code stipulated more diluted ownership concentration, some firms thus being left unable to meet this new standard.

Table 5.1. Characteristics of Listed Kuwaiti Industrial and Service Sector Firms

<table>
<thead>
<tr>
<th>Year</th>
<th>No. of firms</th>
<th>Market capitalisation</th>
<th>Capital value</th>
<th>Traded value</th>
<th>No. of shares outstanding</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td>95</td>
<td>13,857</td>
<td>1,836</td>
<td>5,379</td>
<td>23,930</td>
</tr>
<tr>
<td>2011</td>
<td>95</td>
<td>10,144</td>
<td>2,483</td>
<td>2,825</td>
<td>13,315</td>
</tr>
<tr>
<td>2012</td>
<td>85</td>
<td>9,851</td>
<td>11,174</td>
<td>1,940</td>
<td>14,699</td>
</tr>
<tr>
<td>2013</td>
<td>85</td>
<td>10,145</td>
<td>11,174</td>
<td>2,658</td>
<td>25,576</td>
</tr>
<tr>
<td>2014</td>
<td>87</td>
<td>9,338</td>
<td>14,137</td>
<td>1,634</td>
<td>10,978</td>
</tr>
<tr>
<td>2015</td>
<td>87</td>
<td>7,995</td>
<td>5,203</td>
<td>1,448</td>
<td>9,887</td>
</tr>
<tr>
<td>2016</td>
<td>87</td>
<td>8,964</td>
<td>5,226</td>
<td>951</td>
<td>7,276</td>
</tr>
<tr>
<td>2017</td>
<td>61</td>
<td>8,695</td>
<td>2,476</td>
<td>1,699</td>
<td>8,610</td>
</tr>
</tbody>
</table>


This study considers the approach adopted by the researcher for data analysis, the secondary data analysis being carried out with the implementation in this study. Notably, the robust regression used for the return-on-assets (ROA), return-on-equity (ROE), and Tobin’s Q (TQ) models was chosen over fixed effects, GLS, and OLS regressions for a number of reasons. Here, when ROA, ROE, and TQ (the dependent variables) were treated as continuous variables, the covariance matrices analysis provided no clear link between the variables under examination. There was, however, the presence of a normality problem, whereas the majority of our variables do not normally distribute issues identifiable among the variables (see panels A and B in Table 5.5). Indeed, the presence of an autocorrelation issue, identifiable among the variables (see Table 5.6) and the presence of a heteroskedasticity issue, identifiable among the variables (see Table 5.9) were all seen; furthermore, when we used the Hausman Test, the results indicated the fixed effects regression as being better than GLS (see Table 5.10), while the fixed effects regression results were weak compared to the robust regression (see Table 5.11). Furthermore, the GLS results lacked statistical significance (see Table 5.11). In addition to all of the above, this study also conducted a robustness check for all models the (OLS, GLS, and fixed effects regressions) in Appendix 1, it being found that the robustness for GLS and fixed effects was weak compared to OLS robustness. In light of this, OLS
robustness was used in Table 5.11 as a strong regression as compared to all the regressions completed in Table 5.11 and Appendix 1.

In a similar vein, various measures of firm performance were alternatively regressed on the same set of ownership structure and control variables, these being ROA, ROE and TQ. Notably, ROA and ROE are both common measures of firm performance and indicate how effective a firm is in generating earnings from invested capital (assets and equity, respectively) into net income; furthermore, both can vary substantially, and are highly dependent on the industry; thus, it is typical to compare these against the firm’s own past performance or its peers.

Table 5.2. Kuwaiti Industrial and Service Sector Firms by Industry

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Oil and gas</td>
<td>–</td>
<td>–</td>
<td>8</td>
<td>8</td>
<td>8</td>
<td>8</td>
<td>8</td>
<td>6</td>
</tr>
<tr>
<td>Basic materials</td>
<td>–</td>
<td>–</td>
<td>5</td>
<td>5</td>
<td>5</td>
<td>4</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>Industrial</td>
<td>–</td>
<td>–</td>
<td>39</td>
<td>39</td>
<td>40</td>
<td>39</td>
<td>39</td>
<td>29</td>
</tr>
<tr>
<td>Consumers goods</td>
<td>–</td>
<td>–</td>
<td>7</td>
<td>7</td>
<td>7</td>
<td>8</td>
<td>8</td>
<td>4</td>
</tr>
<tr>
<td>Health care</td>
<td>–</td>
<td>–</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>4</td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td>Telecommunications</td>
<td>–</td>
<td>–</td>
<td>3</td>
<td>3</td>
<td>4</td>
<td>4</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>Technology</td>
<td>–</td>
<td>–</td>
<td>4</td>
<td>4</td>
<td>4</td>
<td>4</td>
<td>4</td>
<td>2</td>
</tr>
<tr>
<td>Consumer services</td>
<td>–</td>
<td>–</td>
<td>16</td>
<td>16</td>
<td>16</td>
<td>16</td>
<td>16</td>
<td>10</td>
</tr>
<tr>
<td>Total</td>
<td>95</td>
<td>95</td>
<td>85</td>
<td>85</td>
<td>87</td>
<td>87</td>
<td>87</td>
<td>61</td>
</tr>
</tbody>
</table>

Note: Categorisation by industry not available for 2010 and 2011.

TQ expresses the relationship between a firm’s market and intrinsic values, and is therefore a way of estimating any overvaluation or undervaluation. Notably, the proxies of ownership structure used here were the proportions of family ownership (FAM), institutional shareholders foreign (ISF), institutional shareholders local (ISL), and government ownership (GOV). Empirical findings elsewhere generally suggest that all four measures are associated with improved firm performance through the professionalisation of investors and their board representatives, improved access to capital, the avoidance of agency costs, and the benefits of closer ties to government through financing and preferential treatment.

Lastly, the control variables were firm size (SZE), leverage ratio (LEV), the debt-to-equity ratio (DET), and cash flow from operating activities (CFO). Generally speaking, larger firms (SZE) are associated with higher firm profitability, better economies of scale, greater corporate diversification, and sustainability (e.g., Fernández et al., 2019; Ibhaugui & Olokoyo, 2018). As found by Fatima and Sohail (2020) and Hussainey and Aljifri (2012), higher risks and thus higher returns, improved debt-avoidant agency costs, boards overpowering managers, lower capital costs and improved firm valuations, and increased
debtholders’ firm performance monitoring (e.g., bondholders, banks) are all associated with higher debt proportions when measured by the $DET$ and $LEV$. Lastly, Ni et al. (2019) found that cash flows ($CFO$) are useful predictors of firm performance through increased capital investment, better liquidity and debt management, cheaper capital, and larger dividends and share repurchases. Table 5.3 details the measurement of each variable mentioned above.

In terms of data sources, firms’ annual financial reports were used to extract the data required for the financial ratios and $TQ$, including net, gross, and operating profit, total revenue and total assets, accounts receivable and short-term investments, along with several second-party databases (i.e., DataStream, Bayanati DataBase). Data available on the KSE (http://www.boursakuwait.com) and Capital Markets Authority Kuwait (http://www.cma.gov.kw) websites were also used. Indeed, Kuwait as a newly developing market, the amount of financial and other information available is noted as being necessarily limited and of short duration.

Table 5.3. Variable Definitions

<table>
<thead>
<tr>
<th>Group</th>
<th>Variable Description</th>
<th>Code</th>
<th>Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent variables</td>
<td>Return-on-assets</td>
<td>ROA</td>
<td>Net income divided by average total assets</td>
</tr>
<tr>
<td></td>
<td>Return-on-equity</td>
<td>ROE</td>
<td>Net income divided by shareholders’ equity</td>
</tr>
<tr>
<td></td>
<td>Tobin’s Q</td>
<td>TQ</td>
<td>Market value divided by replacement cost of the firm assets</td>
</tr>
<tr>
<td>Ownership structure</td>
<td>Family ownership</td>
<td>FAM</td>
<td>Percentage of all shares owned by family</td>
</tr>
<tr>
<td>variables</td>
<td>Institutional shareholders foreign</td>
<td>ISF</td>
<td>Percentage of all shares owned by foreign institutions</td>
</tr>
<tr>
<td></td>
<td>Institutional shareholders local</td>
<td>ISL</td>
<td>Percentage of all shares owned by local institutions</td>
</tr>
<tr>
<td></td>
<td>Government ownership</td>
<td>GOV</td>
<td>Percentage of all shares owned by government</td>
</tr>
<tr>
<td>Control variables</td>
<td>Firm size</td>
<td>SZE</td>
<td>Natural algorithm of total assets at year-end for each firm</td>
</tr>
<tr>
<td></td>
<td>Debt-to equity-ratio</td>
<td>DET</td>
<td>Total liabilities divided by shareholders’ equity</td>
</tr>
<tr>
<td></td>
<td>Leverage ratio</td>
<td>LEV</td>
<td>Long-term debt divided by total assets</td>
</tr>
<tr>
<td></td>
<td>Cash flow from operating activities</td>
<td>CFO</td>
<td>Cash flow from operating activities divided by total assets at start of year</td>
</tr>
</tbody>
</table>

Accordingly, the primary method of the analysis was robust regression-based, using the following model:
\[
FIRM\ PERFORMANCE_{it} = \beta_0 + FAM_{it}\beta_1 + FAM_{it} \times V_t\beta_2 + FAM_{it} \times C_t\beta_3 + ISF_{it}\beta_4 + ISF_{it} \times V_t\beta_5 + ISF_{it} \times C_t\beta_6 + ISL_{it}\beta_7 + ISL_{it} \times V_t\beta_8 + ISL_{it} \times C_t\beta_9 + GOV_{it}\beta_{10} + GOV_{it} \times V_t\beta_{11} + GOV_{it} \times C_t\beta_{12} + SZE_{it}\beta_{13} + DET_{it}\beta_{14} + LEV_{it}\beta_{15} + CFO_{it}\beta_{16} + e_{it}
\]

All the variables are as previously defined and firm performance is ROA, ROE, or TQ. The impact of changing the corporate governance code regime discussed earlier was considered by including the interaction of the corporate governance variables (FAM, ISF, ISL, and GOV) with dummy variables corresponding to the voluntary corporate governance code (V) regime (2013–2015) and the compulsory corporate governance code (C) regime (2016–2017). The estimated coefficients for these (slope) interaction terms then demonstrate not only the impact of the voluntary, then compulsory corporate governance code on firm performance, but also the sources of these changes—whether through family, institutional foreign, institutional local, or government ownership.

5.5 Results

5.5.1 Descriptive Analysis

Table 5.4 provides the mean and standard deviation of firm performance (ROA, ROE, and TQ), ownership structure (FAM, ISF, ISL, GOV), and control variables used in the analysis. With the firm performance measures and relative to the pre-corporate governance code regime, both ROA and ROE increased during the voluntary corporate governance code regime and decreased during the compulsory corporate governance regime. Lastly, TQ decreased in both the voluntary and compulsory corporate governance code regimes.

The ownership structure variables also indicate quite different trends: over all the corporate governance code regimes, FAM represented about 10% of firm ownership and was quite stable across the subsample periods, while ISF accounted for another 5% of ownership. This shows as slow trending-up over time, while ISL decreased during the voluntary corporate governance code regime from 37.5% to 35%, but then increased to 38.2% during the compulsory corporate governance code regime. Lastly, GOV averaged at 6% over all corporate governance code regimes and slowly increased over time.

Lastly, for the control variables, firm size (SZE) trended up over the sample period, while DET increased in both the voluntary and compulsory corporate governance regimes. Meanwhile, LEV decreased in the voluntary corporate governance code regime and then
increased in the compulsory corporate governance regime. On the other hand, the mean cash flows (CFO) decreased greatly in the compulsory corporate governance code regime after remaining stable in the pre- and voluntary corporate governance code regimes, its coefficient of variation indicating (somewhat expectedly) that it was the most variable of the control variables.

Table 5.4. Descriptive Statistics

<table>
<thead>
<tr>
<th>Variable</th>
<th>All corporate governance code regimes</th>
<th>Pre-corporate governance code regime</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>Mean: 2.821 Std. dev: 8.977 Min: 15.71 Max: 35.5 Min: 15.71 Max: 35.5</td>
<td>Mean: 2.610 Std. dev: 9.120 Min: 15.71 Max: 35.5 Min: 15.71 Max: 35.5</td>
</tr>
<tr>
<td>ROE</td>
<td>Mean: 4.612 Std. dev: 17.846 Min: 15.71 Max: 35.5 Min: 15.71 Max: 35.5</td>
<td>Mean: 3.930 Std. dev: 18.802 Min: 15.71 Max: 35.5 Min: 15.71 Max: 35.5</td>
</tr>
<tr>
<td>TQ</td>
<td>Mean: 0.702 Std. dev: 0.527 Min: 0.000 Max: 4.643 Median: 0.574</td>
<td>Mean: 0.688 Std. dev: 0.497 Min: 0.000 Max: 4.643 Median: 0.593</td>
</tr>
<tr>
<td>FAM</td>
<td>Mean: 0.102 Std. dev: 0.170 Min: 0.000 Max: 0.849 Median: 0.000</td>
<td>Mean: 0.103 Std. dev: 0.170 Min: 0.000 Max: 0.849 Median: 0.000</td>
</tr>
<tr>
<td>ISF</td>
<td>Mean: 0.048 Std. dev: 0.152 Min: 0.000 Max: 0.921 Median: 0.000</td>
<td>Mean: 0.050 Std. dev: 0.158 Min: 0.000 Max: 0.921 Median: 0.000</td>
</tr>
<tr>
<td>ISL</td>
<td>Mean: 0.367 Std. dev: 0.255 Min: 0.000 Max: 0.958 Median: 0.367</td>
<td>Mean: 0.375 Std. dev: 0.257 Min: 0.000 Max: 0.958 Median: 0.343</td>
</tr>
<tr>
<td>GOV</td>
<td>Mean: 0.056 Std. dev: 0.142 Min: 0.000 Max: 0.962 Median: 0.000</td>
<td>Mean: 0.063 Std. dev: 0.158 Min: 0.000 Max: 0.962 Median: 0.000</td>
</tr>
<tr>
<td>SZE</td>
<td>Mean: 4.224 Std. dev: 1.449 Min: 0.000 Max: 8.219 Median: 4.114</td>
<td>Mean: 4.163 Std. dev: 1.537 Min: 0.000 Max: 8.159 Median: 4.071</td>
</tr>
<tr>
<td>DET</td>
<td>Mean: 1.132 Std. dev: 3.044 Min: -25.350 Max: 47.725 Median: 0.523</td>
<td>Mean: 1.220 Std. dev: 2.513 Min: 0.000 Max: 25.950 Median: 0.517</td>
</tr>
<tr>
<td>CFO</td>
<td>Mean: 0.065 Std. dev: 0.101 Min: -0.500 Max: 0.711 Median: 0.057</td>
<td>Mean: 0.070 Std. dev: 0.093 Min: -0.300 Max: 0.466 Median: 0.065</td>
</tr>
</tbody>
</table>

5.5.2 Normality Test

Normality in this context being defined as the allocation of residuals within a normal distribution, in order to utilise the parametric assessment, Hair’s (2006) assumption that data must possess a normal distribution to examine hypotheses (despite the fact that this is not required for multiple regression analyses) must be true. Notably, the standardised normal probability plot/P-P normal probability plot, histograms, the quartile of a normal distribution plot/Q-Q normal probability plot, and a kernel density estimate plot are all variations of graphs that can be utilised to showcase the distribution of each variable. Within this particular study, the Shapiro-Wilk test was used, and the variables’ kurtosis and skewness values were also estimated. In this former case, while SZE was the only
one of our variables that did not have a significant p-value, all our variables possessed normality (see Table 5.5), meaning that we should also utilise an alternative regression model so as to study the link between our variables. Notably, it has been suggested that the assumption that normality is present can be undermined when a significant p-value is found, since an insignificant one (i.e., p-value > 0.05) suggests normal distribution (Pallant, 2016). Furthermore, LEV and ISL were our only variables that were shown to be normally distributed via the kurtosis test (see Table 5.5.), a ± 3.29 Kurtosis and a ± 1.96 skewness suggests normality (Field, 2013). Notably, ISF, DET, TQ, and GOV were all found to not possess normal distribution via the skewness test. Therefore, our study sample shows that the data were not normally distributed, which indicated that the other regression such as GLS, fixed effects, and robust should be used rather than OLS.

Table 5.5. Normality Tests

<table>
<thead>
<tr>
<th></th>
<th>Panel A</th>
<th>Panel B (Shapiro-Wilk test)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Skewness</td>
<td>Kurtosis</td>
</tr>
<tr>
<td>ROA</td>
<td>-1.072</td>
<td>8.939</td>
</tr>
<tr>
<td>ROE</td>
<td>-0.586</td>
<td>15.312</td>
</tr>
<tr>
<td>TQ</td>
<td>2.162</td>
<td>12.489</td>
</tr>
<tr>
<td>FAM</td>
<td>1.817</td>
<td>5.768</td>
</tr>
<tr>
<td>ISF</td>
<td>3.840</td>
<td>18.296</td>
</tr>
<tr>
<td>ISL</td>
<td>0.220</td>
<td>2.137</td>
</tr>
<tr>
<td>GOV</td>
<td>3.298</td>
<td>14.571</td>
</tr>
<tr>
<td>SZE</td>
<td>0.072</td>
<td>3.489</td>
</tr>
<tr>
<td>DET</td>
<td>7.134</td>
<td>127.967</td>
</tr>
<tr>
<td>LEV</td>
<td>0.891</td>
<td>2.884</td>
</tr>
<tr>
<td>CFO</td>
<td>0.612</td>
<td>10.131</td>
</tr>
</tbody>
</table>

5.5.3 Autocorrelation

One of the key underlying assumptions for the OLS model is that there is no correlation in terms of the conditional x between different time periods \( \text{Corr}\{u_t, u_s|\text{lx}\} = 0 \) or \( \text{Corr}\{u_t, u_s\} = 0 \), for all \( t \neq s \)—or, in other words, it is assumed that there is no autocorrelation or serial correlation. Indeed, the typical assumption here is that what is likely to occur in time \( t + 1 \) can be forecast based on what occurs in time \( t \) (i.e., the future can be forecasted based off of past events). As stated by Drukker (2003), when it comes to the specific context of autocorrelation, the findings tend to be less reliable, since the standard error is usually underestimated and yet the coefficient estimates are not biased. Indeed, as pointed out by Wooldridge (2013), errors being linked across time will likely lead to their serial correlation if the aforementioned assumption is undermined.
As Drukker (2003) found, the Durbin-Watson test is especially efficient considering it has adapted well to implementation in varying environments, as well as being generally user-friendly—and it is because of this that this was the test utilised within this study with the aim of identifying the serial correlation of OLS models. According to Dufour and Dagenais (1985), a Durbin-Watson value of 2.0 (on a scale ranging from 0 to 4) indicates no autocorrelation within the study sample, despite the fact that the transformed model’s error term is serially independent because it needs to be transformed if it has an autocorrelation issue. Fixed effects, GLS, and robust were notably used in our studies as regressions because we found ROE, ROA, and TQ to be undermined by autocorrelation (see Table 5.6).

Table 5.6. Durbin-Watson Test (Autocorrelation)

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
</tr>
</thead>
<tbody>
<tr>
<td>Durbin-Watson</td>
<td>1.856</td>
<td>1.924</td>
<td>0.480</td>
</tr>
</tbody>
</table>

5.5.4 Correlation Analysis

This section presents the results of the Pearson correlation coefficients, which expose the relationship between ownership structure (i.e., FAM, ISF, ISL, and GOV), firm performance proxies (ROA, ROE, and TQ), and control variables. Previous studies have stated that the higher correlations between independent variables, the more likely it is that a multicollinearity problem exists. Al-Bassam et al. (2018) and Zain et al. (2015) documented higher correlation coefficients are more than ±0.8, and so the existence of multicollinearity problems have the potential to lead to biased research findings, particularly when using the regression models (e.g., OLS). This, in turn, leads to impacts on the capability of regression models in order to detect the association between dependent and independent variables.

Table 5.7 provides the correlation coefficients and their statistical significance. As expected, there was a strong correlation (0.829) between ROA and ROE and moderate correlations between TQ and ROA (0.418) and ROE (0.388), respectively. These results, however, are not supervising, since both ratios measure firm performance levels in Kuwaiti industrial and services firms, and these ratios interact with each other in their formulas. According to other variables, FAM and ISF possess a high correlation (0.99).
Therefore, this study showed that dependent, independent, and control variables correlate with one another, meaning our variables are not free from the multicollinearity issue.

Table 5.7. Correlation Coefficients

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
<th>FAM</th>
<th>ISF</th>
<th>ISL</th>
<th>GOV</th>
<th>SZE</th>
<th>DET</th>
<th>LEV</th>
<th>CFO</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>–</td>
<td>–</td>
<td>.418**</td>
<td>.338**</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>ROE</td>
<td>.829**</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>.090*</td>
<td>.090*</td>
<td>.090*</td>
<td>.090*</td>
<td>.090*</td>
<td>.090*</td>
</tr>
<tr>
<td>TQ</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>.060</td>
<td>.070</td>
<td>.070</td>
<td>.070</td>
<td>.070</td>
<td>.070</td>
<td>–</td>
</tr>
<tr>
<td>FAM</td>
<td>.090*</td>
<td>.060</td>
<td>.070</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>ISF</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>.029</td>
<td>.020</td>
<td>.020</td>
<td>.020</td>
<td>.020</td>
<td>.020</td>
<td>–</td>
</tr>
<tr>
<td>ISL</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>GOV</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>–</td>
</tr>
<tr>
<td>DET</td>
<td>.023</td>
<td>.067</td>
<td>.032</td>
<td>.100*</td>
<td>.100*</td>
<td>.049</td>
<td>.049</td>
<td>.049</td>
<td>.049</td>
<td>.049</td>
<td>–</td>
</tr>
<tr>
<td>LEV</td>
<td>.044</td>
<td>.043</td>
<td>.036</td>
<td>.208**</td>
<td>.208**</td>
<td>.033</td>
<td>.033</td>
<td>.033</td>
<td>.033</td>
<td>.033</td>
<td>–</td>
</tr>
<tr>
<td>CFO</td>
<td>.093*</td>
<td>.076</td>
<td>.084</td>
<td>.198**</td>
<td>.198**</td>
<td>.079</td>
<td>.079</td>
<td>.079</td>
<td>.079</td>
<td>.079</td>
<td>–</td>
</tr>
</tbody>
</table>

Note: Asterisks denote significance at the *** – 0.01, ** – 0.05, and * – 0.10 level.

5.5.5 Variance Inflation Factor (VIF) and Tolerance (1/VIF) Tests

Given the relatively many significant correlations between the independent variables in the analysis comprising the ownership structure and control variables, there is the possibility of multicollinearity—which also brings the possibility of imprecise individual predictors. In order to address this concern, the variance inflation factors (VIFs) were estimated and used to calculate the levels of tolerance (see Table 5.8). The most common rule of thumb is that a VIF > 10 or 5 and tolerance (1/VIF) < 0.1 or 0.2 suggests the presence of harmful multicollinearity, and so, given the mean VIF 1.31, the highest VIF was 1.55 for (ISL), and so the lowest tolerance was 1.09 (CFO), the likelihood of this possibility was rejected.

Table 5.8. VIF and Tolerance

<table>
<thead>
<tr>
<th>Variable</th>
<th>VIF</th>
<th>Tolerance</th>
</tr>
</thead>
<tbody>
<tr>
<td>FAM</td>
<td>1.450</td>
<td>0.689</td>
</tr>
<tr>
<td>ISF</td>
<td>1.140</td>
<td>0.875</td>
</tr>
<tr>
<td>ISL</td>
<td>1.550</td>
<td>0.644</td>
</tr>
<tr>
<td>GOV</td>
<td>1.320</td>
<td>0.756</td>
</tr>
<tr>
<td>SZE</td>
<td>1.280</td>
<td>0.779</td>
</tr>
<tr>
<td>DET</td>
<td>1.210</td>
<td>0.823</td>
</tr>
<tr>
<td>LEV</td>
<td>1.410</td>
<td>0.709</td>
</tr>
<tr>
<td>CFO</td>
<td>1.090</td>
<td>0.915</td>
</tr>
<tr>
<td>MEAN VIF</td>
<td>1.31</td>
<td></td>
</tr>
</tbody>
</table>
5.5.6 Heteroscedasticity Tests

Another potential problem for the regression estimation is heteroscedasticity: statically, heteroscedasticity appears when variable standard deviations are observed over an explicit amount of time (inconstant); or, in other words, it means that the differences of random errors in regression models (e.g., ordinary least square regression [OLS]) are inconstant (Zeng & Tang, 2011; Kaufman, 2013). Consequently, the likelihood of the heteroscedasticity problem increases when the greatness of the residuals seems to be associated to the independent variable value, and overcoming the heteroscedasticity problem can be done by using nonparametric regression, such as white’s robust regression (Rigobon, 2003).

In the analysis, heteroscedasticity tests were performed for the dependent variables in correspondence with the firm performance measures of ROA, ROE, and TQ. Furthermore, there were significant Chi-squared statistics in all cases, but ROA rejected the null hypothesis of homoscedasticity (see Table 5.9). Hence, these results are not surprising, as the firm performance proxies overlap with one another in terms of net income, equality, and assets. Further, ownership structure types are overlapping—particularly managerial and institutional ownership. In conclusion, the heteroscedasticity problem is considered in our ROE and TQ models, this particular research overcoming this problem by using alternative regression such as GLS regression,\(^3\) fixed effect regression,\(^4\) and robust regression.

Table 5.9. Heteroscedasticity Tests

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
</tr>
</thead>
<tbody>
<tr>
<td>(\chi^2(1))</td>
<td>0.270</td>
<td>6.440</td>
<td>75.560</td>
</tr>
<tr>
<td>Prob &gt; (\chi^2)</td>
<td>0.603</td>
<td>0.011</td>
<td>0.000</td>
</tr>
</tbody>
</table>

5.5.7 The Endogeneity Problem

Argued by Elamer and Benyazid (2018), Elshandidy and Neri (2015), Mollah and Zaman (2015), Ntim, Lindop, and Thomas (2013), Ntim and Soobaroyen (2013), and Larcker and Rusticus (2010) to be a very frequently encountered problem in the corporate field, any endogeneity issues—one of the areas that is generally agreed to be best for discussion during the analysis phase—are to be identified within this section. Immeasurable factors

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\(^3\) Not shown in the research since its results are weak compared to robust regression.

\(^4\) Not shown in the research since its results are weak compared to robust regression.
(particularly those linked to the now-eradicated dependent variable), mistakes in the measuring of variables, and the association’s reverse causality are the main reasons the endogeneity issue tends to come about, and the presence of such an issue notably eradicates some of the apprehensions surrounding the type of relationship present and increases the strength of the findings. The Hausman Test, which, as noted by Ozili and Outa (2019), Neifar and Utz (2019), Elamer et al. (2019), Alzeban (2018), and Al-Shaer, Salama, and Toms (2017), shows whether the random-effects model would not be as efficient as the fixed effects model within this particular study, was utilised within this study in order to identify and navigate the endogeneity issue. Indeed, this test is among the most commonly used in this area of research (i.e., the Hausman Test, instrumental variables [3SLS, 2SLS], changing the variables, lagged variables, and the dynamic panel GMM estimator) when navigating the endogeneity problem (Ahmed et al., 2017; Alnabsha et al., 2018; Gong, Xu, & Gong, 2018; Manita et al., 2018; Elamer et al., 2019; Reeb, Sakakibara, & Mahmood, 2020). Indeed, the utilisation of this test allows for the minimising of endogeneity problems and, in turn, the strengthening and stabilising of the research conclusions. In the case of this study, the Hausman Test indicated that the independent variables did not possess endogeneity bias in any of the models, since they had no relationship with the error term (see Table 5.10); furthermore, it also concluded that the fixed effects regression model was more applicable to this research than the random-effects regression model, since all the models’ p-values were documented as being significant.

Table 5.10. Hausman Tests (Endogeneity)

<table>
<thead>
<tr>
<th>Variable</th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
</tr>
</thead>
<tbody>
<tr>
<td>$\chi^2(1)$</td>
<td>13.350</td>
<td>332.750</td>
<td>143.430</td>
</tr>
<tr>
<td>Prob $&gt; \chi^2$</td>
<td>0.100</td>
<td>0.000</td>
<td>0.000</td>
</tr>
</tbody>
</table>

5.5.8 Linearity

In this section, a straightforward relationship between firm performance and ownership structure was sought. Please see Figure 5.1 for a demonstration that such linearity was identified among all of the regression models measuring the relationship between firm performance and ownership structure. Indeed, this result supports the notion that the estimated residual values go against independent variable values (Alghamdi, 2012), and also showcases that the assumption made in this research (i.e., that there would be linearity) was fulfilled.
5.5.9 Outliers

Pinpointing outliers possessing a standard deviation value of over 3, we identified there to be outliers within ROE and ROA—and, in light of this, we completed outlier tests and OLS assumptions within this research to evaluate the regression’s data. Notably, when it comes to examining a typical distribution pattern, around 58 and 50 outliers are expected for ROE and ROA, respectively. Furthermore, any of the outliers identified within our sample (i.e., those with three standard deviations that differed greatly from the mean) required elimination from our analysis in order to guarantee that the undeviating nature was not disrupted. Indeed, the overall findings showcased that there were no improvements to the model once the outliers were substituted by using Winsorising sample data. Notably, these outliers were pinpointed via the standard deviation and mean of the sample. When contrasted with the results garnered from other approaches, our research’s R² and F-value was reduced greatly, and, as supported by Hoaglin and Iglewicz (1987), this indicates that we should resume testing other OLS assumptions with a similar method, considering our outliers were real numbers.

5.5.10 Multivariate Regression Analysis

Family ownership, government ownership, and institutional ownership are the three types of ownership for the Kuwaiti firms listed on the KSE—a different system from those of, for example, the USA, Australia, and the UK. Furthermore, institutional investors, individuals, the government and government agencies, and dominant families are the four types of shareholder within Kuwaiti KSE firms. Notably, a minimal number of major shareholders control and possess such firms, and owners of Kuwaiti firms are frequently highly concentrated. Kim, Pevzner, and Xin (2019), and AL-Qadas, Abidin, and Al-Jaifi
have all studied institutional, familial, and government ownership and concluded there to be a significant relationship between it and firm performance across the countries studied (Italy, 41 different countries, and Malaysia, respectively), despite the fact that the overwhelming majority of previous research conducted in the Middle East within the area tended to neglect to study such types of ownership.

In terms of the estimation technique, robust regression was employed as an alternative to GLS, fixed effects, and OLS regressions, whereby heteroscedasticity and possible contamination of the data with outliers and/or influential observations is present. Notably, the presence of heteroscedasticity has already been proven, and, for the latter, Shapiro-Wilk tests of the normalised residuals squared (to identify outliers in the dependent variables) and leverage (to identify influential observations in the independent variables) were constructed. These normalities (see Table 5.5) indicated that all of the regression models (ROA, ROE, and TQ) possessed relatively many (compared to the mean) observations with high leverage and/or outliers. Further, since there was no compelling reason to exclude these observations from the analysis through data or sampling error, robust regression was deemed appropriate.

Table 5.11 provides OLS, robust, and fixed-effects regression estimates of the performance models in the upper, middle, and lower panels, respectively. All the models were statistically significant, with the F-statistics of the hypothesis showing that all the slope coefficients were jointly insignificant and rejected at the .01 level. As shown by the values of $R^2$, the models explain 27.3%, 28.6%, and 26.6% for ROA, ROE, and TQ, respectively. Meanwhile, the individual coefficient estimates from the robust regression are discussed as the preferred model for ROE and TQ and OLS regression for ROA.

The majority of the prior studies in this area found that a high portion of family ownership led to increased firm performance because they wanted to keep their reputation at the top, as this is more attractive to investors (e.g., Bouzgarrou & Navatte, 2013; Martínez & Requejo, 2017). Table 5.11 demonstrates a positive and significant relationship between $FAM$ and $ROA$ and $TQ$ (2.820 and 2.590, respectively) at level 1%, and $FAM \times V$ and $ROE$ (1.800) at level 10%—indicative of the additional positive effect of family ownership during the early stages of corporate governance reform in Kuwait. These results support Hypothesis 1 and are consistent with the prior literature (e.g., Arouri, et

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5 All regimes (see Table 5.11).
However, the existence of a positive relationship between FAM and firm performance in Kuwait could be referred to keep family investors’ reputation at the top; most family investors are Kuwaiti citizens and they have high loyalty to Kuwait as a country. Table 8 shows that the ROE is positively but insignificantly related to FAM. Possible justification for these results may be in the low level of family ownership on average in Kuwaiti industrial and services firms, which is less than 20% in all model samples (see Table 5.4). Another possible justification is the differences in the measurement of firm performance as a dependent variable in each model.

Institutional ownership is one of the corporate governance characteristics that have received special attention from researchers, since it plays a big role in several business aspects in developed and developing countries. Several prior studies have documented that the institutional investors have played a gradually significant role that affected firm performance, whereas Lin and Fu’s (2017) findings showed a positive relationship between domestic institutional ownership and firm performance in China. This, in turn, enhances shareholder worth by attracting more analysts and reducing insider ownership, which would face difficulty in the financial position. In the same vein, Ferris and Park (2005) found there to be a positive and significant association between forging institutional ownership and firm performance in Japan—and, in light of this, we can see that much of the prior literature agrees that institutional ownership (ISF or ISL) is positively related to firm performance. For example, Chung and Zhang (2011) revealed that a high portion of institutional ownership is more likely to lead to increased governance structure quality, which also leads to increased firm performance quality. This research in particular examines the impact of institutional ownership by dividing it onto ‘domestic’ and ‘foreign’.

Table 5.11 shows there to be no relationship between the firm performance proxies (ROA, ROE, TQ) and ISF at level 10%, results that are not surprising, while the ISF average value in Kuwait is 5%, a figure that is considered to be low compared to ISL 37% (see Table 5.4). Another potential cause for these results could be that the Kuwaiti industrial and services firms suffer from constant change in foreign institutional investors, particularly after the financial crises and revolutions in the Middle Eastern area. This justification is supported by Chung and Wang (2014), although this might also be down to the nature of institutional investors’ culture, since cultural factors play a big role in
motivations. Kuwait, meanwhile, has more than 25 nationalities of institutional investors, particularly since the Middle Eastern revolutions, after which most investors moved their investments to outside of Kuwait (Hamdan & Al-Sartawi, 2013). Finally, the differences between institutional investors’ policies and regulations from country to country are considered to be another possible reason for this (e.g., Al-Bassam et al., 2018; Elyasiani & Jia, 2010). Accordingly, hypothesis 2 is not supported.

In contrast, the estimated coefficients t-statistics in Table 5.11 show there to be a positive and significant relationship between the firm performance proxies ROA, TQ, and ISL (3.700 and 3.080, respectively) at level 1%, and 2.080 at level 5% between ROE and ISL. These results are consistent with those of the prior literature (i.e., Arouri et al., 2014; Du et al., 2014; Hussain, 2015; Tornyeva & Wereko, 2012), meaning H3 is supported. Hence, the agency theory viewpoint advocating that there is a significant relationship between firm performance and ownership concentration via lessened mismatches in incentives and enhanced monitoring is not supported by the findings made here on the grounds of firm performance when measured by ROE, TQ, and ROA.

Finally, government ownership is considered among smaller ownership concentrations in Kuwaiti industrial and services firms (see Table 5.4), whereby the average government ownership is less than 6.5% overall. Indeed, the majority of the prior studies found a high portion of government ownership to be positively related to firm performance proxies. For example, Al-Matari and Al-Arussi (2016) documented government ownership to positively affect firm performance; and, in addition, Al-Matari and Al-Arussi (2016) indicated that government-owned firms’ protection is more likely to reduce any potential errors in firm earnings. Accordingly, we propose there to be a positive relationship between a high portion of government ownership and firm performance in Kuwaiti industrial and services firms. Table 5.11 displays a significant positive association between GOV and firm performance proxies in the sample models ROA and TQ at level 1% (2.050 and 5.190, respectively), and GOV×V and ROE at level 10%, indicating an additional positive effect of government ownership during the early stages of corporate governance reform in Kuwait. These results are consistent with the prior literature (e.g., Alfaraih et al., 2012; Ang & Ding, 2006; Najid & Rahman, 2011). According to our results discussing the relationship between government ownership and firm performance in Kuwaiti industrial and services firms, H4 is supported.
### Table 5.11. Regression Estimates

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>FAM</td>
<td>8.073</td>
<td>2.524</td>
<td>2.820***</td>
<td>10.187</td>
<td>6.511</td>
<td>1.560</td>
<td>0.468</td>
<td>0.195</td>
</tr>
<tr>
<td>FAMxV</td>
<td>6.212</td>
<td>4.048</td>
<td>1.530</td>
<td>16.307</td>
<td>8.100</td>
<td>2.010**</td>
<td>0.178</td>
<td>0.243</td>
</tr>
<tr>
<td>FAMxC</td>
<td>6.381</td>
<td>4.526</td>
<td>1.410</td>
<td>14.655</td>
<td>9.056</td>
<td>1.620</td>
<td>-0.111</td>
<td>0.271</td>
</tr>
<tr>
<td>ISF</td>
<td>-1.385</td>
<td>3.507</td>
<td>-0.390</td>
<td>-5.793</td>
<td>7.018</td>
<td>-0.830</td>
<td>0.191</td>
<td>0.210</td>
</tr>
<tr>
<td>ISxF</td>
<td>0.270</td>
<td>4.728</td>
<td>0.060</td>
<td>5.985</td>
<td>9.462</td>
<td>0.630</td>
<td>-0.251</td>
<td>0.283</td>
</tr>
<tr>
<td>ISFxC</td>
<td>-2.794</td>
<td>6.206</td>
<td>-0.450</td>
<td>-0.070</td>
<td>12.418</td>
<td>-0.010</td>
<td>0.020</td>
<td>0.372</td>
</tr>
<tr>
<td>ISL</td>
<td>7.579</td>
<td>1.925</td>
<td>3.940***</td>
<td>10.743</td>
<td>3.851</td>
<td>2.790**</td>
<td>0.406</td>
<td>0.115</td>
</tr>
<tr>
<td>ISLxV</td>
<td>-1.727</td>
<td>1.849</td>
<td>-0.930</td>
<td>-4.403</td>
<td>3.699</td>
<td>-1.190</td>
<td>0.056</td>
<td>0.111</td>
</tr>
<tr>
<td>ISLxC</td>
<td>-1.711</td>
<td>1.998</td>
<td>-0.860</td>
<td>-1.554</td>
<td>3.999</td>
<td>-0.390</td>
<td>0.159</td>
<td>0.120</td>
</tr>
<tr>
<td>GOV</td>
<td>9.175</td>
<td>3.584</td>
<td>2.560***</td>
<td>8.394</td>
<td>7.172</td>
<td>1.170</td>
<td>0.715</td>
<td>0.215</td>
</tr>
<tr>
<td>GOVxV</td>
<td>4.860</td>
<td>5.304</td>
<td>0.920</td>
<td>11.743</td>
<td>10.615</td>
<td>1.110</td>
<td>0.312</td>
<td>0.318</td>
</tr>
<tr>
<td>GOVxC</td>
<td>-1.156</td>
<td>5.493</td>
<td>-0.210</td>
<td>1.284</td>
<td>10.992</td>
<td>0.120</td>
<td>-0.055</td>
<td>0.329</td>
</tr>
<tr>
<td>SZE</td>
<td>1.335</td>
<td>0.264</td>
<td>5.060***</td>
<td>2.953</td>
<td>0.528</td>
<td>5.590**</td>
<td>-0.015</td>
<td>0.016</td>
</tr>
<tr>
<td>DET</td>
<td>-0.081</td>
<td>0.122</td>
<td>-0.660</td>
<td>-1.257</td>
<td>0.244</td>
<td>-5.140**</td>
<td>0.001</td>
<td>0.007</td>
</tr>
<tr>
<td>LEV</td>
<td>-0.066</td>
<td>0.025</td>
<td>-2.690***</td>
<td>-0.043</td>
<td>0.049</td>
<td>-0.870</td>
<td>-0.007</td>
<td>0.001</td>
</tr>
<tr>
<td>CFO</td>
<td>34.921</td>
<td>3.499</td>
<td>9.980***</td>
<td>62.762</td>
<td>7.001</td>
<td>8.960</td>
<td>1.777</td>
<td>0.210</td>
</tr>
<tr>
<td>Constant</td>
<td>-8.003</td>
<td>1.417</td>
<td>-5.650***</td>
<td>-15.588</td>
<td>2.835</td>
<td>-5.500**</td>
<td>0.491</td>
<td>0.085</td>
</tr>
</tbody>
</table>

Robust regression:

- F-stat/Sig: 13.17*** 0.273 12.580*** 0.286 11.370*** 0.243
- F-stat/Sig: 8.750*** 0.295 7.770*** 0.286 11.090*** 0.266

Robust effects:

- F-stat/Sig: 0.137
- R^2 overall: 1.120 0.057 3.610*** 0.383*** 0.241

Note: Asterisks denote significance at the *** – 0.01, ** – 0.05, and * – 0.10 level.

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137 Chapter 5: Ownership Structure, Corporate Governance Reform, and Firm Performance: Evidence from Kuwait
Family firms typically have lower agency costs and a largely stable level of family ownership (particularly royal family ownership) in Kuwaiti firms, about 10% during the sample period, which all appeared to have had some effect. Likewise, institutional local ownership, averaging about 37% over the sample period but increasing, also significantly affected firm performance. One factor here is that through revolutions and unrest elsewhere, Kuwait is now one of the safer places to invest in the Middle East (Hamdan & Al-Sartawi, 2013). While government ownership in Kuwait remains low (at about 6%), especially when compared with other Gulf states, it likewise has a positive effect on firm performance: for example, Ben-Nasr (2015) argued that this occurs through a reduction in the level of manipulation of financial reports in government-owned firms and the signals this passes to investors. This, however, is expected to change, since the Kuwaiti Government has recently kickstarted a program of partial privatisation through selling down its shareholdings to local and foreign investors.

However, it appears that the Kuwaiti corporate governance code reform has had little positive effect on firm performance—at least in terms of ownership. As discussed, the corporate governance reforms appear substantial, and the fact that these have exerted little positive and no negative effect on the usual impact of firm ownership and different types of ownership suggests that they were, in fact, quite benign. However, a very real alternative is that, as discussed, up to a third of Kuwaiti industrial and service firms exited the market when these reforms became compulsory—largely because they would be unable to meet the new guidelines—suggesting that corporate governance code reforms tend to expel rather than reform potentially noncompliant firms.

Table 5.11 finds SZE to be significant and positive only for the ROE model sample. While this result is consistent with Serrasqueiro and Nunes (2008)—who found that larger firm sizes led to increased firm performance—ROA and TQ showed no relationship between SZE in Kuwait, such a result being consistent with that of Nenova (2003), Agrawal and Knoeber (1996) and Garen (1994).

Since it sways debtors’ and equity shareholders’ partitioning of risk allocation and since it influences the firms’ sensitivity returns on macroeconomic conditions, stock price is expected to be influenced by firm DET (Hutton, Marcus, & Tehranian, 2009). Indeed, when Kuwaiti services and industrial firms’ ROE is at 6.710 at level 1%, DET has been seen to cast significant influence.
According to LEV, Table 5.11 proves to be significant and positive for the ROE model, with 1.810 at level 10% and a significant and negative relationship -3.030 at level 1% with TQ model and no relationship with ROA. These contradictory results could refer to the difference of each firm performance proxies equation structured. Finally, Table 5.11 shows CFO to be positively related to firm performance, whereas ROE is 1.720 at level 10% and TQ is 3.620 at level 1%. These results are consistent with those of the prior literature (e.g. Altman, 2013; Salehi et al., 2017). In addition, the ROA model shows there to be a positive but insignificant relationship between it and CFO, potentially because the focus of the ROA model is on assets items and its close relationship with cash flow.

5.6 Conclusion

This paper explored the relationship between ownership structure (family ownership, foreign and local institutional ownership, and government ownership) and the firm performance proxies (ROA, ROE, and TQ) in Kuwaiti industrial and services firms. Particular focus was paid to the potential impact of the once-voluntary and now-compulsory reforms in Kuwait’s corporate governance code, especially as a market that has lagged behind comparable Gulf economies in this regard.

Institutional, family, and government ownership were all found to exert a positive and significant impact on firm performance, as measured by ROA, ROE and TQ, while forging institutional ownership is not associated with significantly lower (and possibly underutilised) levels of firm performance. Of the four types of ownership in this analysis, institutional local ownership appeared to have the most significant influence on firm performance in terms of both its impact on individual firms and marketwise; this is because of the overall very high level of institutional local ownership in the Kuwaiti market. In contrast, institutional foreign ownership was not associated with levels of firm performance.

Lastly, government and family ownership, while relatively abundant across the market (less than institutional local ownership, but more than institutional foreign ownership), appeared to be influential in increasing the level of firm performance, such that it wielded a positive and significant effect on ROA, ROE, and TQ. In terms of valuation, firms with higher levels of government ownership were the most undervalued, followed by institutional local ownership, family ownership, and, lastly, institutional foreign ownership. Clearly, corporate governance, as reflected by the structure of ownership, has
a pervasive effect on firm performance—at least in Kuwait. Notably, of the four types, institutional local ownership was the most influential on firm performance generally, followed by family ownership and government ownership and, finally, institutional foreign ownership. However, this ranking did not correspond well to the level of ownership, with the exception of institutional foreign ownership; in reality, the levels of family and government ownership in Kuwaiti firms are only about one-quarter and one-sixth of that of institutional local ownership, respectively. However, both have a much stronger impact on firm performance. The obvious rationale is that family, and especially government ownership, is in the form of a single bloc, whereas a large number of investors would be expected to share institutional local ownership with diverse investment horizons and styles.

Perhaps the most interesting finding is that, with just a few exceptions, the corporate governance code reforms that have attracted the most attention in Kuwait (and in neighbouring markets) appear to have had little impact on firm performance. As the reforms are clearly significant as written in terms of their potential impact, this could indicate that most firms already met these guidelines prior to their implementation and that the reforms were therefore generally not required. However, the key insight here is an approximately 30% decline in the number of listed industrial and service sector firms, most from the industrial, consumer goods, and consumer services industries, when the corporate governance code reforms became compulsory. Hence, this implies that, since they were aware that they would not be in a position to fulfil the new rules and regulations, these firms decided to willingly leave the market. As pointed out by Bouresli and Abdulsalam (2019), a key reason for this may be the recent Middle Eastern revolutions, or, alternatively, the new supervisory regulations instilled as a result of new pressures to establish Kuwait as a competitive financial market.

In light of all of the above, several implications have been reached as a result of the current research: we have established that the Kuwaiti Government should be urging those in the institutionally governed listed firms to enrol as members of the board of directors, since local institutional ownership (being one of the KSE’s largest shareholders) has been lauded for its pro-organisational behaviour, which, in turn, has improved firm performance and since this, on a larger scale, could lead to managers and shareholders acting in one another’s best interests more often. We also concluded that minority shareholders should be safeguarded, firm value enhanced, and staff members diversified.
through the proposing of novel policies that cap the amount of authority shareholders have. Additionally, we concluded that skilled and trained shareholders are required for KSE-listed firms, since the issues incurred by the presence of large shareholders with high positions of authority (i.e., the encouragement of an insufficient workspace and environment) would only be emphasised if these shareholders also happened to be inexperienced. Furthermore, foreign investors should be urged to get involved in KSE, and a good relationship between firm performance and ownership should also be encouraged—something that can be done when large shareholders cast a positive influence over managers as a result of high ownership concentration.

Saying this, changes in Kuwaiti corporate governance are always delayed as a result of a range of problems, including decisionmakers’ distraction by recent Middle Eastern revolutions and political tension and tribal chairs influencing decisionmakers for the worst—although these problems should not be considered as the be-all and end-all of corporate governance reformation. Indeed, these issues could be counteracted by regulators directing their attentions to the intangible factors that hinder the changing of ownership structures for the better, such as political tension and cultural issues. To this end, any issues within the current corporate governance can be identified and accounted for via their urging Kuwaiti firm managers to regularly measure the extent to which their team members adhere to the current rules. Such in-depth data concerning corporate governance can also be accumulated via the findings garnered for the first research question within this study, further facilitating their attainment of their firm goals and their formation of productive firm goals.

The conclusion we reached by this research is that the variety of ownership structure adopted largely influences the prominence of the agency problem, such as whether institutional ownership or family ownership is at play. Additionally, it was concluded that the non-executive director’s independence would be guaranteed with additional regulatory initiative, since the governing of shareholders is a job appointed to the directors of public-listed firm with concentrated ownership. Moreover, the elements of ownership structure that require improvement and that also have the potential to enhance firm performance were documented within this study, including the importance of institutional owners when it comes to safeguarding shareholder interests and overall acting in the best interests of the firm. Finally, in spite of the fact that there is not a clear relationship between firm performance and less common types of shareholder, this study has provided
a well-rounded comprehension of the undermining of minority shareholders and the role regulators play in such an event. It was also concluded, as has also been done in a range of other studies, that family-owned businesses are more likely to face agency problems as a result of their lack of sufficient monitoring.

Of course, this analysis is not without its limitations, and these suggest possible future areas of research interest. First, owing to the nature of the Kuwaiti market, the sample period is short (i.e., the period post-corporate governance code and compulsory corporate governance code), and, while the methodology technically addressed these concerns within the context of the analysis, a longer sample period post-corporate governance code and compulsory corporate governance code reform would enable greater surety concerning its long-term impact on firm performance.

Second, while beyond the scope of this analysis, it would be interesting to undertake a detailed examination of the performance of those industrial and service sector firms that exited the Kuwaiti market when the corporate governance code reforms became compulsory, since clearly, these firms anticipated that the costs of meeting the new code and guidelines would exceed any benefit to good corporate governance and retaining the firm’s listing. However, the precise motivation/s remain/s unclear here. Was it because the reforms would have reduced the power of management or restricted internal business dealings with the manager, board members, and employees? Or, alternatively, was it because the reforms required greater disclosure and transparency for both new and potentially past transactions? Regrettably, only a detailed case-by-case analysis is likely to provide a more comprehensive answer to this question, and is potentially limited by the information available.
Chapter 6: The Board of Directors, Audit Committee, and Firm Performance

This chapter comprises a paper prepared as a working paper and submitted for publication in a peer-reviewed journal as follows:

Alajmi, A. and Worthington, A. C. “The Board of Directors, Audit Committee and Firm Performance”, under editorial review at Managerial Finance.

This paper examines the link between board and audit committee characteristics and firm performance in Kuwaiti firms in the context of recent corporate governance reform. Firm performance is measured using returns on assets and equity and Tobin’s Q. The board characteristics include board size, the number of board meetings, and the numbers of independent and outside board members, while the audit committee characteristics include the committee size, the number of committee meetings, and the independence and expertise of the committee members. All board characteristics and the independence and expertise of the audit committee were found to matter for better firm performance, unlike larger audit committees, which were associated with poorer firm performance.

STATEMENT OF CONTRIBUTION TO COAUTHORED PAPER

- The candidate’s contribution to this paper consisted of researching and writing the literature review, formulating and conducting the methodology, analysing and writing up the results, and preparing and formatting the text, tables, and figures.
- Andrew Worthington’s contribution to the paper involved guiding the research design and editing.
6.1 Introduction

The two separate but related organisational structures key to firms’ corporate governance are boards of directors and audit committees, the former being largely responsible for firm performance and ensuring the development and implementation of strategies and policies that enable the firm to perform for the benefit of shareholders. These are usually implemented on a day-to-day basis through delegation to management, which the board also monitors and supports on a constant basis; however, boards are also responsible for the firm’s compliance with its legal, regulatory, and industry obligations through ensuring the organisation develops and implements appropriate systems, processes, and procedures for this purpose.

Problematically, these dual roles of performance and compliance can present a dilemma for boards, which primarily flows from the necessarily future orientation of the performance role and the past and present focus of the compliance role, the differing external emphases of the performance role on strategy and the compliance role on accountability, and the dissimilar internal applications of the performance role to policymaking and the compliance role to monitoring and supervision. It is for this reason that audit committees were created as a delegated, specialised, and independent committee of the board of directors to assist boards in serving their compliance role.

Boards of directors clearly have the greatest impact on overall firm performance, with desirable features of boards, board members, and board meetings in this regard being their dedication to the task, their expertise and knowledge, and their independence and freedom from conflicts of interest (Bhagat & Bolton, 2019); however, audit committees also have a role to play, partly in enabling the board to appropriately perform its overall compliance role and ensuring that it not only meets its mandated obligations to external parties, but is also able to manage the firm’s risks from its activities.

There is, however, another aspect of audit committees in that they provide an internal service in monitoring and supervising the firm, as well as an external service in assisting investors in making confident and informed decisions (Burke et al., 2019), both of which potentially and additionally affect firm performance. In addition, in much the same way as boards, audit committees, along with the quality of their audits, are a function of their understanding of the business and assessment of the risks to the firm, the expertise of the audit committee members, and their effectiveness and engagement. It is this that formed the motivation for this study; that
is, one studying boards of directors and audit committees as they work both separately and together, with a view to good governance and better firm performance.

This study is particularly interested in the developing market contexts, where many corporate governance frameworks, principles, and practices are only slowly developing and their relationships are still evolving. The commensurate lack of previous empirical attention to this arena is blatantly obvious, and, to this end, one particularly interesting context is Kuwait: a small but highly influential economy among the GCC member states. Despite this, Kuwait was slow among its neighbours to develop a general corporate governance code and guidelines, and only adopted its first in 2013. Further to this, the firms listed on the KSE are now subject to two sets of regulations: capital markets authority laws (dating from 2010 and which used to regulate the behaviour of market participants), and firm (so-called ministry) laws (dating from 2016). Together, these laws imposed many corporate governance articles and provisions newly obliging all listed firms to make necessary changes to their bylaws and internal policies, while for boards, they included a minimum number of board members, the separation of the board chair and chief executive officer, a minimum number of board meetings, regulations governing executive and non-executive members, and a requirement for independent directors. For audit committees, meanwhile, they included a minimum number of audit committee members and meetings, the requirement for members to hold professional certification, the designation of roles not permitted to meet with internal and external auditors, and a requirement for independent members.

Nearly as interestingly, the implementation of these requirements was staggered: prior to 2013 and until 2015, there was no corporate governance code or guidelines—only voluntary compliance, and, from 2016 onwards, there was compulsory compliance. This represents a unique natural experiment in whether the foreshadowed shift to an at first voluntary, then compulsory, corporate governance code and guidelines involved different impacts of boards of directors and audit committees on firm performance.

The motivation for this analysis stems from its providing insight into the factors that are recognised to influence the link between corporate governance and firm performance, particularly each country’s own legal and cultural practices and social environment. This will assist investors (both local and foreign in the country) and government officials, market regulators, and accounting professionals in devising future investment, industry, and regulatory policies. This is particularly the case in Kuwait, with the country being very much focused on
significantly improving the attractiveness of its investment environment, and, thereby, the flow of capital by enhancing the quality of governance in its listed firms.

Any research concerning the nature of the relationship between firm performance and corporate governance has taken place in the context of the Middle East. With this in mind, since this particular investigation offers information concerning Kuwait’s abundance of materials, Kuwait has been an area of much interest for investors compared to others in the Middle East. To this end, the objective of this particular study is to establish the nature of the relationship between Kuwaiti industrial and services firms’ performance and the implemented corporate governance mechanisms.

The current research has yielded some results that contribute significantly to the current literature within this field. A major reason for this is the fact that it accounts for any potential hindrances to the implemented mechanisms’ growth and room for development in Kuwait—a factor that the majority of the current literature neglects to investigate. This also, as is perhaps expected, facilitates a more detailed understanding of the hindrances that could be faced by boards of directors and audit committees. Furthermore, this research adds to the current literature because it takes place in a developing country, unlike the overwhelming majority of the other research in this field—and, more specifically, it takes place within the Kuwaiti context, a country that was, before this study, yet to be investigated in this field. In turn, our selection of Kuwait as our context for the research has the potential to allow the country’s academics to take into account any of the flaws in this study when conducting their own research. Additionally, considering that the vast majority of Kuwaiti firms are currently still being built (as is usually the case with developing countries), this research and its findings could allow such business owners to bear in mind the findings of this research and put their best foot forward when beginning to conduct business. This research will also inevitably aid Kuwaiti market regulators, investors, accountants, and government officials when it comes to formulating new policies and making plans for the country’s economic future. Finally, this study will be of great value to the people of Kuwait when considering the fact that the topic of corporate governance has been gaining more and more attention in this country as time has gone on; thus, this is a highly relevant piece of research, particularly in the wake of the Kuwaiti Government recently adopting its first Capital Markets Authority.

The remainder of this paper is structured as follows: Section 6.2 discusses the related literature and derives the hypotheses to be tested, Section 6.3 details the methodology, Section 6.4 explains the results, and Section 6.5 provides the chapter’s conclusion.
6.2 Literature and Hypotheses

Well-established theory and the relevant ensuing empirical literature have both established the positive link between good corporate governance and improved firm performance—and, through that, provided a benefit to shareholders and other stakeholders. For instance, Pahi and Yadav (2019) argued that the paying of dividends was positively associated with strong corporate governance, while Forte and Tavares (2019) suggested a similar relationship with short- and long-term debt and, thus, firm liquidity and financial risk. From this, subsequent research has considered the different components of the corporate governance framework—typically boards of directors and less often audit committees (almost never both), and their respective contributions.

In this chapter, this rich literature and the characteristics of the structures thought to impact upon the quality of good governance—and therefore firm performance—are considered. For example, Safari (2017) revealed that strong boards of directors and audit committee compliance leads to a reduction in earnings management in firms, while Arayssi, Jizi, and Tabaja (2020) concluded that board independence and gender improved the quality of firm financial goals. Meanwhile, Alhajri (2017) suggested that boards were interested in auditing as a means of improving the quality of financial reporting. Discussion of how best to define firm performance is presented in Section 6.3.

6.2.1 Board Characteristics and Firm Performance

The extant literature suggests that the relationship between corporate governance and firm performance is a function of several board characteristics, including board size, insider and independent board membership, and board member experience, along with the regulatory, cultural, economic, and political environment in which they operate (Bhagat & Bolton, 2019; Mertzanis et al. 2019). To start, board size is critical in reflecting the collective experience and expertise of the board, as well as its ability to counter the performance-inhibiting power of management and other insiders and non-independent board members.

According to Sonnenfeld (2002) and Lipton and Lorsch (1992), agency theory maintains that there is a positive relationship between firm performance and small boards, while there is a negative one between firm performance and larger boards. This conclusion was reached by Lipton and Lorsch (1992) as they considered the fact that in smaller boards, directors are in a position to discuss their thoughts openly and transparently during meetings, which leads to smaller boards being more consistent in their thought processes and decisions. Furthermore, it
has been assumed that large boards are more likely than small boards to use up materials more quickly, since larger boards automatically require more funding than their smaller counterparts. Furthermore, it has been maintained that more productivity is typically attained within smaller boards, since the agency problem is thought to be more abundant in large boards (Yawson, 2006). Finally, it has also been supposed that larger boards are more likely than smaller boards to be manipulated by CEOs as a result of associated director avoidance, and can also be more difficult to manage (Jensen, 1993).

On the other hand, the likes of Yawson (2006) and John and Senbet (1998) argue that, through the lens of agency theory and resource-dependency theory, there may be a positive relationship between firm performance and a large board. According to Yawson (2006), larger boards are associated with better management in terms of overseeing employees and decision-making, since a wider scope of skillsets is likely to be present. Furthermore, as stated by Haniffa and Hudaib (2006), a more diversified array of contacts, business opportunities, skillsets, and resources is likely to be accessible when a large board is employed. Additionally, as founded by Kiel and Nicholson (2003), inappropriate manager decisions are more likely to be stood up against in larger boards because there is a wider range of personality and skillset present, in turn, as pointed out by John and Senbet (1998), resulting in improved monitoring within the firm. Finally, Goodstein, Gautam, and Boeker (1994) and Pearce and Zahra (1992) maintain that materials such as raw materials, contracts, and finances are more likely to be obtained within larger boards, since such boards allow for easier access to the external world and, thus, minimise risk and uncertainty within the workplace. Regardless of the nature of the relationship between these two factors, it is indisputable that board size is greatly influential within businesses in terms of their performance, and, as a result, this has been the topic of much research within the field.

Bhagat and Bolton (2019), for example, concluded there to be a significant positive relationship between board size and firm performance in the USA, while Upadhyay (2015) suggested that board size also helped to determine capital structure with an equity discount in firms with larger boards and more long-term debt. To add to this, Aktan et al. (2018) found there to be a positive relationship between board size and Return on assets (ROA) as a proxy of firm performance in Bahrain. In the same vein, Al-Matari et al. (2014b) documented board size to positively and significantly impact Tobin’s Q (TQ) as a proxy for firm performance in Oman. In contrast, using a sample of 1,502 Chinese listed firms during the period 2008–2013, Haider and Fang (2016) concluded there to be a negative association between board size and firm risk, such that
smaller boards necessarily performed better. Furthermore, several prior studies found board size to be negatively related to firm performance (e.g., Ahmed, Hossain & Adams, 2006 [New Zealand]; Al-Matari et al., 2012a [Kuwait]; Mak & Kusnadi, 2005 [Singapore and Malaysia]; Pillai & Al-Malkawi, 2018 [GCC]). Elsewhere, Hoseini et al. (2019) found that board size significantly impacted upon tax avoidance in Iran, which in turn directly and positively related to the level of firm performance. Finally, Aljifri and Mustafa (2007) found no relationship between board size and firm performance in the UAE.

The number of board meetings may notably also impact firm performance, also reflecting the frequency and timeliness of firm decision-making and monitoring. According to Vafeas (1999), there is a positive relationship between sufficient management and frequent board meetings within a firm, since, according to Khan, Muttakin, and Siddiqui (2013) and Mahadeo, Soobaroyen, and Hanuman (2012), the board of director’s main task is to oversee the firm’s mechanisms. This notion is backed by Schwartz and Weisbach (2013), who indeed maintain that there is a positive relationship between firm performance and frequent board meetings, since this alleviates the agency problem.

According to Vafeas (1999) and Conger et al. (1998), agency theory maintains the stance that the regularity of board meetings ultimately establishes a given board’s quality and participation in firm activities. In the same vein, it has been pointed out that a proficient manager can usually be identified by how frequently board meetings are held (Sonnenfeld, 2002)—and, according to Mangena et al. (2012), managers will be in a better position to make well-informed decisions within the workplace when there are frequent board meetings, as such meetings will provide employees with the opportunity to keep managers up-to-date with the goings-on of the firm. Indeed, Vafeas (1999) also points out that formulating strategies, evaluating firm performance, and productive conversations are all likely to take place more efficiently with frequent board meetings. Finally, Lipton and Lorsch (1992) conclude that casual day-to-day correspondences combined with frequent board meetings can result in better relationships and communication between board members.

Meanwhile, some researchers (e.g., Vafeas, 1999) suggest that regular board meetings are not necessarily required for shareholders. Conversely, some researchers have proposed that a business system that is efficient in quickly addressing issues as they arise would be more advantageous for firms than regular board meetings, for example increasing the number of meetings held in accordance with how well the firm is performing (Jensen, 1993), particularly when considering a lot of expenses arise with frequent board meetings. Furthermore, according
to Lipton and Lorsch (1992), how much time directors have available to oversee managers is reduced because managers usually do not discuss matters of high relevance, thus suggesting that frequent board meetings would not necessarily always be productive (Vafeas, 1999). Indeed, both Jensen (1993) and Vafeas (1999) are in agreement when it comes to the notion of a ‘sweet spot’ of the number of board meetings conducted on a firm-by-firm basis, rather than simply scheduling a large number of board meetings that could end up being unproductive.

The existing literature concerning the association between the frequency of board meetings and firm performance is largely mixed; for example, in Indonesia, Tanjung (2020) concluded that board meetings were positively related to enhancing the studied firms’ financial performance, while in China, Ji, Talavera, and Yin (2020) documented that more board meetings led to an increase in the quality of governance, which, in turn, also increased the growth of strategies related to IPO proceeds and firm performance. Similarly, Min and Chizema (2018) highlighted that regular board meetings with high levels of attendance were significant when assessing corporate governance effectiveness, while Fletcher and Ridley (2018), using an interventionist approach, found that the performance mentality of the board had a significant relationship with management accounting information and its timely delivery to the board. Lastly, DeBoskey, Luo, and Zhou (2019) investigated the impact of the effectiveness of board oversight on the tone of earnings announcements using board meetings as a proxy, and found that frequent meetings reduced the aggressiveness and improved the optimism of earnings announcements, and ultimately translated into better firm performance. As agency theory takes the stance that frequent board meetings would improve shareholder-manager relationships and communication, it has been concluded that there is a positive relationship between firm performance and regular board meetings (Schwartz & Weisbach, 2013). This result was consistent with that of Ntim and Osei (2011), as well as that of Bhargava and Faircloth (2014), whose study was conducted in the USA context.

Conversely, some researchers have concluded there to be a negative relationship between firm performance and regular board meetings (i.e., Aktan et al., 2018; Al-Matari et al., 2014b; Fich & Shivdasani, 2012; Hassan, Naser, and Hijazi, 2016; Vafeas, 1999). Fama and Jensen (1983a) have also been clear on their stance that a firm’s financial performance will be reduced with frequent board meetings as a result of expenses for travel, meetings, etc. Further, it has also been pointed out that a rise in agency costs would be likely with regular board meetings (Vafeas, 1999).
Firm performance and corporate governance are also thought to be improved with board independence—that is, the inclusion of directors who have no money-related incentives concerning the business. Such a notion is supported by Fama and Jensen (1983a), since such directors usually possess such skillsets and contacts that this could only be beneficial to the firm. Furthermore, according to Fama (1980), agency theory takes the stance that agency problems will only be alleviated with the impartiality of outside directors; to this end, it could be argued that a high number of independent directors could increase firm performance as a result of additional monitoring (Goodstein et al., 1994). Black et al. (2006) also maintain that, indeed, reduced agency problems are normally witnessed in independent boards. Finally, the likes of Gordini (2012), Baranchuk and Dybvig (2009), and Haniffa and Hudaib (2006) maintain that all the evidence of agency theory points towards board independence as being directly correlated to improved firm performance.

Despite the above, the studies conducted concerning the nature of the relationship between firm performance and board independence have yielded rather mixed results. Srairi (2015) documented there to be a positive relationship between the 27 studied Islamic banks’ performance (ROE, ROA) and board independence. Such a result is supported by that of three other studies, where researchers concluded there to be a positive relationship between their studied firms’ performance and board independence (Bravo & Reguera, 2017; Garefalakis, Dimitras, & Lemonakis, 2017; Pearce & Patel, 2018). Notably, Al-Najjar (2014) similarly documented the existence of a positive relationship between their studied tourism firms’ performance (ROA) and board independence, this also being the case for Anis et al.’s (2017) 70 studied firms.

While Kavitha et al. (2019) revealed there to be a positive relationship between the proportion of independent directors and discretionary disclosures within Indian firms, Alipour et al. (2019) similarly documented that board independence displayed a significant positive association with firm performance via the quality of environmental disclosure. Further, concerning capital structure, Tosun and Senbet (2020) demonstrated that board independence tended to improve the internal monitoring system as a means of better controlling firm debt maturity in both the long and short term. Meanwhile, Meder et al. (2018) concluded that the level of board independence facilitated the early repayment of debt, and, in so doing, reduced the risk of bankruptcy. In other work, Lu and Wang (2018) linked board independence with corporate innovation, while Sena et al. (2018) found board independence was likely to reduce the negative impact of firm corruption.
On the other hand, Bozec (2005) investigated 25 Canadian firms from 1976 to 2000 measured by ROA, return on sales and Tobin’s $Q$, and found that firm value was lower in firms that had a board dominated by independent board members. Meanwhile, Al-Maghzom, Hussainey, and Aly (2016) found there to be no significant association between the two variables, while more recently, Molnar, Wang, and Chen (2017) also found there to be no significant relationship between the independent board and firm performance. In the context of Kuwait country, it was found in one study that there was a negative relationship between firm performance ($TQ$) and board independence, and that this relationship ran only from board independence to firm performance (Al-Saidi, 2020).

Lastly, an outside director is a member of a board of directors not selected from within the firm, and so, outside directors are arguably more objective than insiders. They can also bring different perspectives and skills to the management of a firm. According to Jensen (1993), Lipton and Lorsch (1992), and Fama (1980), the implementation of board outsiders is, according to past research, the most efficient way of alleviating the agency problem in the context of corporate governance. Notably, the evidence most frequently used in support of board outsiders is that garnered from stewardship theory and agency theory, which will both be explored below.

While board outsiders bring three key things to the table, agency theory, according to Sonnenfeld (2002) and Fama (1980), implies that diminished accountability is usually seen in firms with boards possessing executive directors. These three things are as follows: as stated by Baranchuk and Dybvig (2009) and Haniffa and Hudaib (2006), the valuable factors are knowledge, reputation, experience, and contacts; according to Fama and Jensen (1983b) and Fama (1980), the guarantee that board outsiders are behaving in the way they should through the presence of both internal and external managerial markets; and finally, according to Chhaochharia and Grinstein (2009) and the Cadbury Report (1992), external and unbiased opinions to board decision-making. It could be argued that shareholders are more likely to be undermined and competitive relationships to become unhealthy with internal managers taking up all of the key roles within a given firm (Fama, 1980; Fama & Jensen, 1983b).

Along these same lines, Black et al. (2006) maintain that information asymmetry is likely to be reduced and shareholder investments to be protected with the implementation of board outsiders within a given firm, since, as articulated by Jensen (1993), external individuals are less likely to hold back with their criticisms and opinions in the name of politeness, conflict and avoidance than those within the firm. Furthermore, according to Fama and Jensen (1983b),
such implementation also reflects well on business owners, since it indicates they are open to feedback and want to make decisions that are genuinely in the best interests of the firm. Indeed, the notion that opportunistic behaviour will be decreased with the employment of such board outsiders is backed by Fama (1980); and, as a whole, a wealth of researchers, as can be seen from the above, are of the opinion that the more board outsiders are employed, the better firm performance is bound to become.

Saying this, advocates of stewardship theory, such as Bozec (2005), Weir and Laing (2000), and Baysinger and Hookisson (1990), maintain there to be a negative relationship between firm performance and board outsiders. Jiraporn et al. (2009) and Bozec (2005) state that board outsiders typically only work part-time and also contribute to other firms’ boards, meaning they only have a limited amount of time to commit to the board at hand, which only serves to emphasise Weir and Laing’s (2000) point that outsiders will frequently not understand enough about the business whose board they are a part of to make any valuable contribution to decisions. Furthermore, reduced firm performance could be predicted for those employing board outsiders since their likely lesser knowledge would mean they provide very little high-quality advice. This is compounded by Haniffa and Hudaib’s (2006) conclusion that managers’ strategy-driven decisions may be jeopardised by board outsiders in cases where such outsiders govern much of the firm. However, Nicholson and Kiel (2007) maintain that more productive decisions are likely to be reached with the extra information board outsiders are sure to bring, which, of course, would only serve to improve board performance.

Prior literature that concerned board outsiders and firm performance provided mixed results: Maseda et al. (2015) investigated the relationship between outsiders on the board and revealed a positive relation with firm performance, especially in family firms, while Stein and Zhao (2019) linked outsiders not only with better firm performance, but also with lower CEO compensation and higher earnings quality. Further, Lai, Chen, and Song (2019) concluded that outsiders improved the quality of information made available to investors, while Pombo and Gutiérrez (2011) suggested that a high portion of board outsiders led to increased asset returns in non-financial firms. Adams and Jiang (2016) went on to employ six different proxies to reflect the beneficial impact of outsiders on board decision-making, and, lastly, Arosa et al. (2010) suggested that outside directors could act as either agents or stewards, with both roles serving to improve firm performance. In the context of GCC, a few studies found that board outsiders positively related to firm performance (e.g., Al-Matari et al., 2012a [Kuwait]; Al-Matari et al., 2014b [Oman]).
Indeed, some studies, including those by Haniffa and Hudaib (2006), Weir and Laing (2000), Vafeas and Theodorou (1998), and Hermalin and Weisbach (1991) all conclude there to be no significant identifiable relationship between firm performance and board outsiders. Meanwhile, the likes of Bozec (2005), Laing and Weir (1999), Agrawal and Knoeber (1996), and Yermack (1996) all conclude there to be a negative relationship between firm performance and the percentage of outsiders present. One such study conducted in the Nigerian context surmised that outsiders could be a problem to managers because they are too involved, despite the fact that they do also bring some benefits (e.g., objectivity, knowledge, independence) (Sanda et al., 2010). Another study also concluding there to be a negative relationship between these two factors was notably conducted in the Canadian context (Bozec, 2005).

In reflection of these prior theories and literature, the following four hypotheses were proposed:

\[ H1: \text{There is a positive relationship between board size and firm performance.} \]

\[ H2: \text{There is a positive relationship between the number of board meetings and firm performance.} \]

\[ H3: \text{There is a positive relationship between the level of board independence and firm performance.} \]

\[ H4: \text{There is a positive relationship between the number of board outsiders and firm performance.} \]

### 6.2.2 Audit Committee Characteristics and Firm Performance

The importance of audit committees stems from their main responsibilities: supervising firm management, overseeing the internal and external auditors to reduce financial errors, providing the public including investors and regulators with accurate information, and protecting shareholders. The existing literature has particularly identified audit committees as being the corporate governance tool that is most focused on mitigating fraudulence in financial statements (Al-Baidhani, 2014; Burke et al., 2019). For the most part, the quality of this governance role can be proxied using the size of the audit committee, the frequency of its meetings, and the independence and expertise of its members.

Audit committee size is, indeed, widely recognised as one characteristic that is most associated with business decision-making. Furthermore, according to Obiyo and Lenee (2011), Nuryana and Islam (2011), and Hsu and Petchsakulwong (2010), audit committee size, an essential aspect of corporate governance, is typically measured by the number of members that are on-
board, the Kuwaiti Government outlining that firms must possess at least three audit committee members. As is maintained by Mohid, Mohd, and Mohd (2009) and Klein (2002), a proficient audit committee is required in order to alleviate Fama and Jensen’s (1983b) agency problem, which in this context arises from subpar control mechanisms and managers undermining shareholders’ interests. To expand on this, Jensen and Meckling (1976) outline that through the lens of agency theory, the misalignment of interests between shareholders and managers typically results in managers making decisions that are incentivised by their own interests, in turn undermining those of shareholders. Meanwhile, as explained by Pearce and Zahra (1992) and Pfeffer (1973), resource-dependency theory maintains that efficient audit committees are usually characterised by individuals who swap ideas and knowledge in pursuit of fulfilling shareholder interests, and, in line with this, states that larger audit committees are more beneficial to firms as a result of the wider scope of skillsets likely to be present.

One relevant study indeed finding there to be a positive relationship between a large audit committee and firms’ financial reporting (Felo, Krishnamurthy, & Solieri, 2003), it is unanimously agreed that audit committee size is hugely influential when it comes to financial reports and, in turn, a given firm’s overall performance—although research findings are usually rather mixed. Some of these are explored below.

The likes of Bagais and Aljaaidi (2020) and Al-Matari et al. (2012a), who conducted their studies in Saudi Arabia and Kuwait respectively, have documented the existence of a positive relationship between firm performance (ROA) and audit committee size. Other research yielding similar results includes that of Yasser, Entebang, & Mansor (2011), who concluded there to be a positive relationship between firm performance (ROE) and audit committee size within their study sample; and, further to this, Kyereboah, Adjasi, and Abor (2007) similarly documented the existence of a positive relationship between their 103 studied Kenyan, South African, Ghanaian, and Nigerian firms’ performance and audit committee size. Other researchers who found there to be a positive relationship between these factors include Hamdan et al. (2013), Swamy (2011), Heenetigala and Armstrong (2011), Reddy, Locke, and Scrimgeour (2010), Premuroso and Bhattacharya (2007), and Khanchel (2007). However, Sultana, Singh, and Rahman (2019) proposed that audit committee size was positively linked with audit quality, while Li, Mangena, and Pike (2012) used a sample of UK-listed organisations to reveal the positive effect of audit committee size on the firm’s intellectual capital. Several studies have investigated the effect of audit committee size on earnings
management, revealing that audit committee size limits earnings management across firms (e.g., Inaam & Khamoussi, 2016).

While Al-Matari et al. (2014b) and Mak and Kusnadi (2005) concluded there to be no significant identifiable relationship between firm performance and audit committee size (in Oman and Malaysia and Singapore, respectively), the likes of Hsu and Petchsakulwong (2010), Moilah and Talukdar (2007), and Bozec (2005) have all concluded there to be a negative relationship between firm performance and audit committee size.

The frequency of audit committee meetings is another characteristic that could potentially impact firm performance. Kuwait’s corporate governance code stipulates that audit committees should hold a minimum of four meetings annually, and, according to Alqatamin (2018), Raghunandan and Rama (2017), and He et al. (2009), firm performance is bound to improve the more audit committee meetings are held, since the monitoring of management is bound to improve with these. Saying this, it still stands that the vast majority of the research within this field has yielded varied findings. One such study by Al-Matari et al. (2012b) concluded there to be a positive relationship between Saudi Arabian firms’ performance and regular audit committee meetings, which supports agency theory’s notion that this relationship is, indeed, positive (Fama & Jensen, 1983a). Furthermore, another study conducted in 2010 concluded there to be a positive relationship between the 223 studied US firms’ performance (Tobin’s Q) and regular audit committee meetings (Hsu & Petchsakulwong, 2010).

Using a Jordanian sample of firms, Alzoubi (2019) documented that the more audit committee meetings increased, the better the overall quality of financial reporting for the firm. Moreover, Alzeban and Sawan (2015) stated that one of the roles of the audit committee is to review and monitor management’s response to internal audit findings and recommendations. Further, frequent meetings also benefited internal audit implementation and recommendations. In the same vein, Kalelkar (2016) examined whether firms increased their audit committee monitoring during auditor change and its putative benefits, and found this to be in the affirmative. Lastly, using a sample of 118 listed financial and non-financial firms, Hoque et al. (2013) found the frequency of audit committee meetings to be positively related to firm performance, particularly in terms of ROA and equity.

Meanwhile, some other studies have concluded there to be a negative relationship between firm performance and frequent audit committee meetings. One such study found there to be a negative relationship between quarterly earnings management and frequent audit committee
meetings (Yang & Krishnan, 2005), while another found there to be a negative relationship between Saudi Arabian firms’ performance and frequent audit committee meetings (Bagais & Aljaaidi, 2020). Further to this, a study conducted in 2012 documented the existence of a negative relationship between firm performance (ROA) and audit committee meeting frequency (Aldamen et al., 2012), while another similarly found there to be a negative relationship between Oman firms’ performance and regular audit committee meetings (Al-Matari et al., 2014b).

Meanwhile, a study conducted in 2014 concluded there to be no significant identifiable relationship between the 112 studied non-financial Jordanian firms’ performance and regular audit committee meetings (Kikhia, 2014), while another conducted three years later found the same results for firms in the UAE (Farhan, Obaid, & Azlan, 2017). This same result was concluded by Hamdan et al. (2013), while another also concluded there to be no significant identifiable relationship between the studied 165 non-financial Jordanian firms’ performance and audit committee characteristics (Alqatamin, 2018). What we can conclude from the aforementioned studies and their results is that findings certainly differ depending on the geographical context of the research.

With the implementation of an audit committee, independent directors are able to frequently oversee managers and ensure that no opportunistic behaviour is occurring, and, thus, we can see here that audit committees (and audit committee independence) play a central role in effective corporate governance. As stated by Carcello and Neal (2003), corporate governance is, in a roundabout way, backed by audit committee members, as they encourage good financial reporting, because their key responsibility is to guarantee honesty in such reporting (Uddin & Choudhury, 2008). Indeed, their effectiveness is evidenced in the fact that the Australian corporate governance principles and recommendations outline that audit committees must have a minimum of three independent directors. While some are of the opinion that better monitoring, financial reporting, and transparency can be achieved with a large number of independent directors within a given audit committee (Beasley, 1996; Bronson et al., 2009; Carcello & Neal, 2000; Prentice & Spence, 2006), others take the view that opportunistic behaviour is just as likely to occur regardless of whether a large number of independent directors are present (Romano, 2005). The question of which opinion is more valid remains largely unanswered by the existing research, whose findings are rather varied.

Mohamed, Ahmad, and Sulaiman (2014) have stated that the amount of fraud that occurs within a given firm could be significantly minimised with a fair audit committee, and it could also be
argued that better overall firm performance and audit reporting could be attained with such an audit committee (Arslan et al., 2014; Bouaziz & Triki, 2012). It is also important to note that a given audit committee’s independence is absolutely critical, since it is that which will prevent opportunistic behaviour from managers (Cohen et al., 2011), and, as pointed out by Sarkar (2013), elements such as net income, total income, and equity are all likely to be noticed and taken account of by independent members of audit committees. In terms of the research backing such notions, one study found there to be a positive relationship between the studied Nigerian firms’ financial performance and independent audit committees, concluding that these committees helped reduce financial oversights (Ilaboya & Obaretin, 2015). Similarly, another study found there to be a positive relationship between the studied Pakistan firms’ financial performance and audit committee independence (Yasser et al., 2011). Indeed, another researcher stated in 2008 that there is a positive relationship between having a higher number of independent directors on an audit committee and firm financial reporting (Dey, 2008). Notably, Al-Matari et al. (2014b) also found there to be a positive relationship between the studied Oman financial firm performance and independent members of audit committees.

In a comparative study of India and GCC countries, Al-ahdal et al. (2020) revealed that audit committee factors significantly affect firm performance in all countries—and, noting this, the results for the India sample showed better results compared to GCC countries. Notably, independence also has a role in audit committees, Perez et al. (2019) postulating that committee independence improves firm reputation and therefore value. Meanwhile, Schrader and Sun (2019) stated that greater audit committee independence would likely to lead to an increase in the quality of firms’ and employees’ compensation, as did Moses (2019), who studied a sample of Nigerian firms between 2009 and 2018. Further, Poretti, Schatt, and Bruynseels (2018) documented that audit committee independence positively related to more than 7,600 earnings announcements between 2006 and 2014 across 15 European countries. On this basis, they concluded that audit committee independence was essential for firms to convey their credibility to investors and other stakeholders. Finally, audit committee independence is important to audit quality within firms, with Gebrayel et al. (2018) finding that high audit committee independence ultimately resulted in higher quality financial reports.

Conversely, while the likes of Kajola (2008) and Cotter and Silvester (2003) have documented there to be no significant identifiable relationship between firm performance and audit committee independence, others, such as Ghabayen (2012), Ibrahim, Raman, and Saidin
Audit committee members’ individual and collective expertise (i.e., their educational background) is another element of corporate governance, and audit committees more specifically, that is thought to significantly influence firm performance, with the Kuwaiti Government outlining that at least one audit committee member must have experience—whether that be work experience or educational qualifications—in finance and/or accounting. As maintained by Abbott, Parker, and Peters (2004), it is critical that all firms follow such a rule and ensure that some members have experience in these arenas, despite the fact that diversity is normally prioritised within audit committees. To add to this, Al-Matari et al. (2014a) state that employing audit committee members who have sufficient experience should be a high priority to managers. Through the lens of resource-dependency theory, the likes of Bedard, Chtourou, and Courteau (2004) and McDaniel et al. (2002) concluded from their research results that there is a significant relationship between firm performance and audit committee expertise—a conclusion that aligns with Pfeffer and Salancik’s (2003) view that education is an external resource that particularly impacts firms’ financial performance. With this in mind, it could be argued that having members who are fluent in financial reporting (and finances in general), auditing, and internal control is actually necessary for an audit committee’s success (Oncioiu et al., 2020); after all, audit committees are primarily responsible for all auditing and financial reporting, and so it seems sensible to conclude that team members need to be well versed in the topics at hand (Lin, Xiao, & Tang, 2008).

One study in this area did, indeed, find there to be a positive relationship between firm performance and audit committee members’ expertise (DeFond et al., 2005), with another study supporting this result by corroborating that more qualified team members are more efficient with decision-making and monitoring management than those who are not as qualified, in turn enhancing firm performance (Hillman & Dalziel, 2003). It has also been found that firms that are currently performing badly should prioritise taking on financially and/or technically experienced members (Carcello & Neal, 2003). Overall, research findings concerning the relationship between firm performance and audit committee members’ expertise is fairly mixed.

Lee and Park (2019) examined the relationship between audit committees’ expertise and textual information conveyed via management discussion, ultimately finding that high audit committee expertise led to the improvement of several firm concerns, including the quality of
management decisions and the compliance of the firm with regulations and legislation. Meanwhile, Chen and Komal (2018) used a meta-analysis of 165,529 observations from some 90 studies, to reveal that audit committee expertise generally improved the quality of financial reporting. Further to this, Baxter and Cotter (2009) stated that audit committee expertise was an important corporate governance mechanism that improved financial report quality using a sample of Chinese firms. Lastly, Sultana and Mitchell (2015) argued that audit committee expertise was important in recognising the asymmetrical timeliness of losses and an essential tool affecting earnings conservatism.

Notably, a wealth of studies have documented there to be a positive relationship between these two factors. One such study conducted in Australia documented there to be a significantly positive relationship between the 300 studied Australian firms’ performance and audit committee members’ educations and expertise (Aldamen et al., 2012). Yang and Krishnan (2005) found there to be a significant positive relationship between reducing the 250 studied US firms’ internal control issues and financial expertise among audit committee members. While another similar study by Hamid and Aziz (2012) found there to be a positive relationship between these two factors when the audit committee members had financial expertise.

Conversely, some of the research in the literature has documented there to be a negative relationship between these two factors. One such study investigating its sample between 2001 and 2008 indeed documented there to be a negative relationship between the studied UK firms’ performance (ROA) and audit committee financial expertise (Badolato et al., 2014), while another found these two factors to have a negative relationship (Liu, Tiras, & Zhuang, 2014). Another study concluded that there was no significant identifiable relationship between the 165 studied Amman non-financial firms’ incomes and audit committee members with high levels of education (Alqatamin, 2018), while another stated there to be a negative relationship between firm performance and the audit committee possessing independent members with financial expertise (Abbott et al., 2004). Finally, another study documented there to be no significant identifiable relationship between the studied UAE firms’ performance and audit committee expertise (Farhan et al., 2017).

Given all of the above, the following four hypotheses were proposed in relation to audit committee characteristics and firm performance:

$$H5: \text{There is a positive relationship between audit committee size and firm performance.}$$
\[ H6: \text{There is a positive relationship between the number of audit committee meetings and firm performance.} \]

\[ H7: \text{There is a positive relationship between the level of audit committee independence and firm performance.} \]

\[ H8: \text{There is a positive relationship between the level of audit committee expertise and firm performance.} \]

6.3 Model Specification

In order to test hypotheses H1 to H8, board of directors and audit committee characteristics were used as proxies for corporate governance mechanisms, and an independent variable was used in order to improve firm performance (PRF) as a dependent variable in the following regression model:

\[
P_{RF} = \alpha_0 + \beta_1BSZ_{it} + \beta_2BMT_{it} + \beta_3BIN_{it} + \beta_4BOU_{it} + \beta_5ASZ_{it} + \beta_6AMT_{it} \\
+ \beta_7AIN_{it} + \beta_8AEX_{it} + \beta_9AST_{it} + \beta_{10}DTE_{it} + \beta_{11}LEV_{it} + \beta_{12}CFO_{it} \\
+ \beta_{13}COM_{it} + \beta_{14}VOL_{it} + \varepsilon_{it}
\]

The sample comprised an unbalanced panel of 682 firm-years for between 61 and 95 Kuwaiti industrial and service firms operating over the period 2010–2017. All data was derived from the KSE and DataStream and drew upon the discussion on the Kuwaiti corporate governance reform and the missing values of some firms concerning the sample period (2010–2017) with 520 firm-year observations as a net sample. Considering that they have rather distinctive and uncommon corporate governance mechanisms, with different rules and regulations compared to other firms, insurance and financial firms were not included in this study sample, which was instead limited to Kuwaiti services and industrial firms. Other studies that did not include financial firms within their own samples include those of El-Faitouri (2014), Amran (2012), and Haniffa and Hudaib (2006). Table 6.1 details the variable measurements.
Table 6.1. Variable Definitions

<table>
<thead>
<tr>
<th>Variable</th>
<th>Label</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firm performance measures</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Return-on-assets</td>
<td>ROA</td>
<td>Net income divided by average total assets</td>
</tr>
<tr>
<td>Return-on-equity</td>
<td>ROE</td>
<td>Net income divided by shareholders’ equity</td>
</tr>
<tr>
<td>Tobin’s Q</td>
<td>TQ</td>
<td>Market value of firm divided by replacement value of firm assets</td>
</tr>
<tr>
<td>Board of directors characteristics</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board size</td>
<td>BSZ</td>
<td>Number of board directors elected by shareholders</td>
</tr>
<tr>
<td>Board meetings</td>
<td>BMT</td>
<td>Number of annual board meetings</td>
</tr>
<tr>
<td>Board independence</td>
<td>BIN</td>
<td>1 if CEO and board chairman are same person; otherwise 0</td>
</tr>
<tr>
<td>Board outsiders</td>
<td>BOU</td>
<td>Number of nonexecutives on board divided by total board members</td>
</tr>
<tr>
<td>Audit committee characteristics</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Audit committee size</td>
<td>ASZ</td>
<td>Number of committee members elected by board directors</td>
</tr>
<tr>
<td>Audit committee meetings</td>
<td>AMT</td>
<td>Number of annual committee meetings</td>
</tr>
<tr>
<td>Audit committee independence</td>
<td>AIN</td>
<td>1 if committee comprises only nonexecutive members; otherwise 0</td>
</tr>
<tr>
<td></td>
<td></td>
<td>1 if all committee members qualified and at least one has an accounting professional certificate; otherwise 0</td>
</tr>
<tr>
<td>Audit committee expertise</td>
<td>AEX</td>
<td></td>
</tr>
<tr>
<td>Control variables</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm size</td>
<td>AST</td>
<td>Natural logarithm of year-end total assets</td>
</tr>
<tr>
<td>Debt-to-equity ratio</td>
<td>DTE</td>
<td>Total liabilities divided by shareholders’ equity</td>
</tr>
<tr>
<td>Leverage ratio</td>
<td>LEV</td>
<td>Long-term debt divided by year-end total assets</td>
</tr>
<tr>
<td>Cash flow</td>
<td>CFO</td>
<td>Cash flow from operating activities divided by year-beginning total assets</td>
</tr>
<tr>
<td>Voluntary corporate governance code and guidelines regime</td>
<td>VOL</td>
<td>Dummy variables that take 1 if the years of study sample is corporate governance voluntary</td>
</tr>
<tr>
<td>Compulsory corporate governance code and guidelines regime</td>
<td>COM</td>
<td>Dummy variables that take 1 if the years of study sample is corporate governance compulsory</td>
</tr>
</tbody>
</table>

6.3.1 Firm Performance

Several different approaches served to measure firm performance in comparable corporate governance studies. These revolved around measuring firm performance by focusing on the different major areas of firm decision-making: the capital structure method, which focuses on capital structure; the financial management method, which focuses on both investment and cash flow; the firm outcome recourses method, which concerns financing; and the sustainable growth method, which is a combination of investing, operating, and financing. Each of these performance measures is relevant in terms of assessing the impact of good corporate governance fostered by desirable board and audit committee characteristics, and, hence, specifying them alternatively in the current model as the dependent variable (PRF) highlights different avenues through which good corporate governance translates to better firm performance.
6.3.2 Board and Audit Committee Characteristics

The board of directors’ characteristics proxied the quality of corporate governance in the firm and reflected the four main variables used in the prevailing literature: board size; the number of board meetings, and the number of independent and outsider directors on the board. These were specified as independent variables, against which \( PRF \) was regressed as variously measured (either \( ROE \), \( ROA \), or \( TQ \)). For each year, board size (BSZ) was specified using the number of board directors elected by shareholders (+) and board meetings (BMT) with the number of annual board meetings (+) (expected coefficient sign in brackets). Board independence (BIN) was a dummy variable taking a value of one if the CEO and board chairperson were the same person; otherwise, it was zero (+), while board outsiders (BOU) was the number of non-executives on the board divided by total board members (+).

Audit committee characteristics for the firms and for each year of the sample were also specified, audit committee size (ASZ) being specified using the number of committee members elected by the board of directors (+) and audit committee meetings (AMT) with the number of annual committee meetings (+). Audit committee independence (AIN) was a dummy variable that took a value of one if the committee comprised only non-executive members (otherwise zero [+]), and audit committee expertise (AEX) was a dummy variable that took a value of one if all committee members were qualified and at least one has an accounting professional certificate, otherwise zero (+).

6.3.3 Control Variables

In addition to the board of directors and audit committee characteristics, a number of control variables were also specified in the performance model for completeness (Adams & Jiang, 2016; Kalelkar, 2016); unfortunately, however, as Kuwait is a developing market, the availability of this information is limited, and is a possible limitation of this analysis—a fault that is readily acknowledged. To start, most existing studies recognise that firm size is an important factor generally affecting firm performance; however, firm size and corporate governance also potentially relate, given the fact that larger firms generally have more agency problems, thus requiring the integration of strong governance mechanisms (Pillai & Al-Malkaw, 2018). That being said, the opportunities and prospects for financial manipulation are very much reduced in this case. Firm size (AST) was measured using the natural logarithm of year-end total assets and a positive sign hypothesised when specified as a regressor for firm performance.
Other corporate governance – firm performance research suggests debt-to-equity and leverage also determine better firm performance, particularly those in countries with strong corporate governance codes and regulations, and possibly due to the greater oversight of more complex organisational structures (Fatima & Sohail, 2020; Hussainey & Aljifri, 2012; Mohamad & Sulong, 2010). Debt-to-equity (DTE) was measured by total liabilities divided by shareholders’ equity, while leverage ratio (LEV) was measured by long-term debt divided by year-end total assets. Lastly, high cash flow from operating activities (CFO) was also more likely to lead to an increase in firm performance, in turn attracting more investors (e.g., Andreas, 2017). This was measured using cash flow from operating activities divided by year-beginning total assets.

Additionally, two dummy variables were used to proxy the corporate governance code and regulations in place at the time of the analysis. As discussed, Kuwaiti firms have been subjected to three different regulatory regimes during the sample period from 2010 to 2017: no corporate governance code from 2010 to 2012, voluntary compliance with the new corporate governance code from 2013 to 2015, and compulsory compliance with the new corporate governance code from 2016 onwards. Consequently, the dummy variable of voluntary corporate governance code and guidelines (VOL) took a value of one for firm observations in 2014 and 2015 (otherwise zero), while compulsory corporate governance code and guidelines (COM) took a value of one in 2016 and 2017 (otherwise zero).

The pre-corporate governance code and guidelines in operation in 2010, 2011, and 2012 provided the reference category; assuming the new corporate code and guidelines had a material effect on the quality of governance over and above the board of directors and audit committee characteristics described earlier, the hypothesis was for positive signs for both VOL and COM. However, firms with good or less good corporate governance may have been early movers or late adopters of the new code and guidelines, in which case the significance and magnitudes of the coefficients for VOL and COM could vary.

Finally, this study considers the approach adopted by the researcher for data analysis, the secondary data analysis being carried out with the implementation in this study. The robust regression was notably used for the ROA, ROE, and TQ models, and these were chosen over fixed effects, GLS, and OLS regressions for a number of reasons: for one, when ROA, ROE, and TQ (the dependent variables) were treated as continuous variable, the covariance matrices analysis provided no clear link between the variables under examination. Further, there was the presence of correlation and multicollinearity problems, whereas some of our variables have these problems, identifiable among the variables (see Tables 6.3 and 6.4); the presence of
autocorrelation issue, identifiable among the variables (see Table 6.7); and the presence of the heteroskedasticity issue, identifiable among the variables (see Table 6.5). Additionally, when we used the Hausman Test, the results indicated that the fixed effects regression model was better than GLS for the ROE and TQ models, and the GLS regression was better than fixed effects for the ROA model (see Table 6.8). Saying this, the fixed effects and GLS regression results were weak compared to robust regression (see Table 6.9 and Appendix 2).

6.4 Results

6.4.1 Descriptive Analysis

Table 6.2 details the means, maximum, minimum, standard deviations, and coefficients of variation for the three dependent performance variables and the 12 board of directors, audit committee, and control (excepting VOL and COM) independent variables. As expected, the mean ROE (4.612) exceeded the mean ROA (2.821). When it comes to how the measured variables performed, TQ measured at 0.751, ROE at 3.869, and ROA at 3.182. The magnitudes of the performance variables were broadly consistent with similar work in the Middle East outside Kuwait, including that of Qasim (2014), Pamburai et al. (2015), and Kallamu (2016).

Table 6.2. Descriptive Statistics

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Max</th>
<th>Min</th>
<th>Std. dev.</th>
<th>CV</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>2.821</td>
<td>33.515</td>
<td>-48.645</td>
<td>8.977</td>
<td>3.182</td>
</tr>
<tr>
<td>ROE</td>
<td>4.612</td>
<td>135.613</td>
<td>-103.750</td>
<td>17.846</td>
<td>3.869</td>
</tr>
<tr>
<td>TQ</td>
<td>0.702</td>
<td>4.643</td>
<td>0.000</td>
<td>0.527</td>
<td>0.751</td>
</tr>
<tr>
<td>BSZ</td>
<td>5.935</td>
<td>10.000</td>
<td>0.000</td>
<td>1.357</td>
<td>0.229</td>
</tr>
<tr>
<td>BMT</td>
<td>6.113</td>
<td>13.000</td>
<td>0.000</td>
<td>1.988</td>
<td>0.325</td>
</tr>
<tr>
<td>BIN</td>
<td>0.121</td>
<td>1.000</td>
<td>0.000</td>
<td>0.327</td>
<td>2.702</td>
</tr>
<tr>
<td>BOU</td>
<td>0.891</td>
<td>1.000</td>
<td>0.000</td>
<td>0.117</td>
<td>0.131</td>
</tr>
<tr>
<td>ASZ</td>
<td>1.044</td>
<td>6.000</td>
<td>0.000</td>
<td>1.537</td>
<td>1.472</td>
</tr>
<tr>
<td>AMT</td>
<td>1.340</td>
<td>11.000</td>
<td>0.000</td>
<td>2.132</td>
<td>1.591</td>
</tr>
<tr>
<td>AIN</td>
<td>0.302</td>
<td>1.000</td>
<td>0.000</td>
<td>0.460</td>
<td>1.523</td>
</tr>
<tr>
<td>AEX</td>
<td>0.296</td>
<td>1.000</td>
<td>0.000</td>
<td>0.457</td>
<td>1.544</td>
</tr>
<tr>
<td>AST</td>
<td>4.224</td>
<td>8.219</td>
<td>0.000</td>
<td>1.449</td>
<td>0.343</td>
</tr>
<tr>
<td>DTE</td>
<td>1.132</td>
<td>47.725</td>
<td>-25.350</td>
<td>3.044</td>
<td>2.689</td>
</tr>
<tr>
<td>LEV</td>
<td>16.652</td>
<td>62.240</td>
<td>0.000</td>
<td>16.300</td>
<td>0.979</td>
</tr>
<tr>
<td>CFO</td>
<td>0.065</td>
<td>0.711</td>
<td>-0.500</td>
<td>0.101</td>
<td>1.554</td>
</tr>
</tbody>
</table>

Note: CV–coefficient of variation.

In terms of the corporate governance characteristics, the typical Kuwaiti board had nearly six board members (BSZ = 5.935), met about six times each year (BMT = 6.113), and had about 12% of its members as independents (BIN = 0.121) and 89% as outsiders (BOU = 0.891). These appeared broadly compliant with the adoption of the Kuwaiti corporate governance code,
which took effect in only half of the sample years and required a given board to have at least five directors meeting at least once every two or three months, a majority of non-inside members, and at least one-third independent members. Further, while there was significant variation in the proportion of inside directors based on its coefficient of variation ($BIN = 2.702$), the remaining board of director characteristics were much less so ($BSZ = 0.229$, $BMT = 0.325$, and $BOU = 0.131$). This could suggest that most Kuwaiti firms were compliant with the new corporate governance code throughout the full sample period, even before its suggested or mandatory adoption, apart from the requirements governing inside directors.

Turning to the audit committees, the average Kuwaiti firm had an audit committee with slightly more than one member ($ASZ = 1.044$), meeting an average of once per year ($AMT = 1.340$), with only one-third being fully independent ($AIN = 0.302$)—that is, only non-executive members—and one-third meeting the criteria for expertise ($AEX = 0.296$). In contrast to the statistics of the boards of directors, the relatively large coefficients of variation for all four variables are suggestive of the significant changes in the audit committee characteristics among Kuwaiti firms over the period in question ($ASZ = 1.472$, $AMT = 1.591$, $AIN = 1.523$, and $AEX = 1.544$). More importantly, they also fell far short of the requirements set by the Kuwait corporate governance code, such that audit committees should have no less than three non-executive members and meet at least four times a year. Together, this suggests that the recently adopted corporate governance code has had a potentially greater influence on corporate governance through the conduct and composition of the audit committees than the boards of directors.

Overall, it was noticed that all of the board of directors and audit committee characteristics have zero value of their minimum, which means that some firms in Kuwait do not comply with the new corporate governance code. Finally, the descriptive features of the four firm-level control variables were considered, and, as shown, the average firm in the current sample had assets ($AST = 4.22$) in natural logarithms equating to some 68 million Kuwaiti dinars (KD) ($\approx$ USD$224$ million), with debt-to-equity ($DTE$) and leverage ($LEV$) average values of (1.132, 16.652) respectively. Meanwhile, cash flow from operating activities ($CFO$) was just above three million KD ($\approx$ USD$3.5$ million). Of the four control variables, $DTE$ and $CFO$ clearly involved the most variability across time and firms based on their coefficients of variations 2.689 and 1.554, respectively.
6.4.2 Correlation, Multicollinearity, and Heteroscedasticity

As a partial test of the potential for harmful multicellularity in the regression analysis to follow, as well as to investigate the statistically significant pairwise associations between variables, Table 6.3 provides the Pearson correlation coefficients between the performance, board of directors, audit committee, and control variables. This study reveals the results of such Pearson correlation coefficients, which expose the relationship between board of directors’ characteristics, audit committee characteristics, and firm performance proxies (ROA, ROE, and TQ) in Table 3. Notably, prior literature has stated that higher correlations between variables are likely to suggest the existence of a multicollinearity problem. On this note, Al-Bassam et al. (2018) documented higher correlation coefficients as being more than ±0.8. Subsequently, the existence of a multicollinearity problem could lead to bias in the findings of any research, particularly when using regression models (e.g., OLS). This, in turn, led to impacts in regards to the capability of regression models in detecting the association between dependent and independent variables. For the alterative performance measures (and as expected), there was a high relation between ROE and ROA (0.829)—an unsurprising result, considering these two variables interact with each other in terms of net income. However, several independent variables—particularly audit committee characteristics—correlate with each other according to the relationship between all of them together: for example, ASZ, AMT, AIN, and AEX have high positive associations with one another, which is not surprising, as committees of a larger size are more likely to be expected to have independent members with more regular meetings. Lastly, all other independent and control variables have no high relationship between them, and, according to Table 6.3, this study has suffered with the multicollinearity problem.
Table 6.3. Correlation Coefficients

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
<th>BSZ</th>
<th>BMT</th>
<th>BIN</th>
<th>BOU</th>
<th>ASZ</th>
<th>AMT</th>
<th>AIN</th>
<th>AEX</th>
<th>AST</th>
<th>DTE</th>
<th>LEV</th>
<th>CFO</th>
<th>COM</th>
<th>VOL</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ROE</td>
<td>0.829**</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>TQ</td>
<td>0.418**</td>
<td>0.338**</td>
<td>1.000</td>
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<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>BSZ</td>
<td>0.094*</td>
<td>0.104*</td>
<td>0.185**</td>
<td>1.000</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>BMT</td>
<td>-0.035</td>
<td>-0.045</td>
<td>-0.005</td>
<td>0.013</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<td></td>
</tr>
<tr>
<td>BIN</td>
<td>0.171**</td>
<td>0.178**</td>
<td>0.206**</td>
<td>0.131**</td>
<td>-0.164**</td>
<td>1.000</td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>BOU</td>
<td>-0.031</td>
<td>-0.014</td>
<td>0.058</td>
<td>0.233**</td>
<td>0.120**</td>
<td>-0.179**</td>
<td>1.000</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AMT</td>
<td>0.023</td>
<td>0.045</td>
<td>-0.048</td>
<td>0.072</td>
<td>0.357**</td>
<td>-0.176**</td>
<td>0.075</td>
<td>1.000</td>
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</tr>
<tr>
<td>AIN</td>
<td>-0.007</td>
<td>0.009</td>
<td>-0.058</td>
<td>-0.105*</td>
<td>0.353**</td>
<td>-0.181**</td>
<td>0.090*</td>
<td>0.907**</td>
<td>1.000</td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AEX</td>
<td>0.022</td>
<td>0.021</td>
<td>-0.050</td>
<td>-0.015</td>
<td>0.323**</td>
<td>-0.193**</td>
<td>0.072</td>
<td>0.922**</td>
<td>0.870**</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>AST</td>
<td>0.017</td>
<td>0.021</td>
<td>-0.018</td>
<td>0.019</td>
<td>0.315**</td>
<td>-0.176**</td>
<td>0.059</td>
<td>0.903**</td>
<td>0.834**</td>
<td>0.885**</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>DTE</td>
<td>-0.059</td>
<td>-0.204**</td>
<td>-0.121**</td>
<td>-0.001</td>
<td>0.001</td>
<td>0.024</td>
<td>0.055</td>
<td>0.066</td>
<td>0.071</td>
<td>0.073</td>
<td>0.065</td>
<td>0.196**</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>LEV</td>
<td>-0.103*</td>
<td>-0.070</td>
<td>-0.300**</td>
<td>0.111*</td>
<td>-0.032</td>
<td>-0.014</td>
<td>0.077</td>
<td>-0.019</td>
<td>0.020</td>
<td>0.011</td>
<td>-0.027</td>
<td>0.354**</td>
<td>0.373**</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CFO</td>
<td>0.450**</td>
<td>0.427**</td>
<td>0.375**</td>
<td>0.124**</td>
<td>-0.068</td>
<td>0.072</td>
<td>0.067</td>
<td>-0.003</td>
<td>-0.022</td>
<td>-0.012</td>
<td>-0.025</td>
<td>0.148**</td>
<td>-0.126**</td>
<td>-0.121**</td>
<td>1.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>COM</td>
<td>-0.013</td>
<td>0.003</td>
<td>0.003</td>
<td>-0.008</td>
<td>0.021</td>
<td>0.058</td>
<td>-0.009</td>
<td>-0.077</td>
<td>-0.065</td>
<td>-0.060</td>
<td>-0.044</td>
<td>-0.023</td>
<td>-0.071</td>
<td>0.010</td>
<td>-0.035</td>
<td>1.000</td>
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<tr>
<td>VOL</td>
<td>0.030</td>
<td>0.027</td>
<td>0.018</td>
<td>0.026</td>
<td>0.018</td>
<td>-0.032</td>
<td>0.027</td>
<td>-0.015</td>
<td>-0.029</td>
<td>0.001</td>
<td>-0.033</td>
<td>0.053</td>
<td>0.041</td>
<td>-0.008</td>
<td>-0.010</td>
<td>-0.447**</td>
<td>1.000</td>
</tr>
</tbody>
</table>

Note: Asterisks denote significance at the *** – 0.01, ** – 0.05, and * – 0.10 level.

To better examine the potential for harmful multicollinearity, the variation inflation factors (VIFs) and tolerances are calculated in Table 6.4. Generally, VIFs with a value of less than 10 and tolerances more than 0.2 suggest no serious multicollinearity, and, as shown in Table 6.4, these criteria were met for all independent variables except audit committee size, which had a VIF of 11.98 and a tolerance of 0.083. However, as these only marginally failed to meet the criteria (and given the average VIF across all variables was just 3.21), there was little prospect for harmful multicollinearity overall.
Table 6.4. VIFs and Tolerance

<table>
<thead>
<tr>
<th>Variable</th>
<th>VIF</th>
<th>Tolerance</th>
</tr>
</thead>
<tbody>
<tr>
<td>BSZ</td>
<td>1.320</td>
<td>0.758</td>
</tr>
<tr>
<td>BMT</td>
<td>1.200</td>
<td>0.836</td>
</tr>
<tr>
<td>BIN</td>
<td>1.130</td>
<td>0.881</td>
</tr>
<tr>
<td>BOU</td>
<td>1.170</td>
<td>0.858</td>
</tr>
<tr>
<td>ASZ</td>
<td>11.980</td>
<td>0.083</td>
</tr>
<tr>
<td>AMT</td>
<td>6.130</td>
<td>0.163</td>
</tr>
<tr>
<td>AIN</td>
<td>8.280</td>
<td>0.121</td>
</tr>
<tr>
<td>AEX</td>
<td>6.110</td>
<td>0.164</td>
</tr>
<tr>
<td>AST</td>
<td>1.460</td>
<td>0.684</td>
</tr>
<tr>
<td>DTE</td>
<td>1.210</td>
<td>0.829</td>
</tr>
<tr>
<td>LEV</td>
<td>1.350</td>
<td>0.739</td>
</tr>
<tr>
<td>CFO</td>
<td>1.100</td>
<td>0.912</td>
</tr>
<tr>
<td>COM</td>
<td>1.280</td>
<td>0.778</td>
</tr>
<tr>
<td>VOL</td>
<td>1.280</td>
<td>0.783</td>
</tr>
<tr>
<td>MEAN VIF</td>
<td>3.210</td>
<td></td>
</tr>
</tbody>
</table>

One problem, however, that is very likely to arise when using firm-level data is heteroscedasticity, particularly when combining cross-sectional and time-series data, as was done here. The Breusch–Pagan/Cook–Weisberg was used to test for heteroscedasticity and the $\chi^2$, and Table 6.5 shows that values (p-values in brackets) were significant only for $TQ = 83.120$ (<0.001), but not $ROA$ and $ROE$—a result that indicates that this is, indeed, mostly the case. This would conventionally be addressed using nonparametric regression, but for this analysis, robust regression was selected.

Table 6.5. Heteroscedasticity Tests

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
</tr>
</thead>
<tbody>
<tr>
<td>$\chi^2(1)$</td>
<td>0.100</td>
<td>2.210</td>
<td>83.120</td>
</tr>
<tr>
<td>Prob &gt; $\chi^2$</td>
<td>0.750</td>
<td>0.138</td>
<td>0.000</td>
</tr>
</tbody>
</table>

6.4.3 Normality Test

As stated by Black (2001) and Cooke (1998), the data has to be distributed normally in order for normality to be assumed, and, while it has been maintained that small inconsistencies in normality do not tend to impact findings (Jackson, 2014) and that a consistently normal distribution of data is actually rather rare (Gujarati & Porter, 1999), according to Coakes and Steed (2009), inconsistencies in data do not need to be worried about. Indeed, from this—as well as from the fact that Brooks (2019) also maintained that the undermining of the normality assumption is of little importance—it seems sensible to take that stance that, in this study (i.e., one exploring 520 firms), the meeting of the normality assumption should not be a massive priority, as was concluded by Ntim,
Nevertheless, the normality test was still implemented in this study using the Shapiro-Wilk test and the skewness and kurtosis values. In terms of the former, a significant value (i.e., one smaller than 0.05) indicates the normality assumption’s being undermined which we have to use other regressions rather OLS (Pallant, 2016), while for the latter, a skewness value of +/-1.96 and a kurtosis value of +/-3.29 are considered to confirm normality. All the gathered results for each proxy can be seen in Table 6.6.

Table 6.6. Normality Tests

<table>
<thead>
<tr>
<th></th>
<th>Panel A</th>
<th></th>
<th>Panel B (Shapiro-Wilk Test)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Skewness</td>
<td>Kurtosis</td>
<td>Z. Stat</td>
</tr>
<tr>
<td>ROA</td>
<td>-1.072</td>
<td>8.939</td>
<td>8.616</td>
</tr>
<tr>
<td>ROE</td>
<td>-0.586</td>
<td>15.312</td>
<td>10.082</td>
</tr>
<tr>
<td>TQ</td>
<td>2.162</td>
<td>12.489</td>
<td>9.514</td>
</tr>
<tr>
<td>BSZ</td>
<td>0.683</td>
<td>4.325</td>
<td>6.034</td>
</tr>
<tr>
<td>BMT</td>
<td>0.954</td>
<td>5.206</td>
<td>7.238</td>
</tr>
<tr>
<td>BIN</td>
<td>2.322</td>
<td>6.392</td>
<td>5.299</td>
</tr>
<tr>
<td>BOU</td>
<td>-2.095</td>
<td>15.310</td>
<td>10.304</td>
</tr>
<tr>
<td>ASZ</td>
<td>0.892</td>
<td>2.065</td>
<td>7.477</td>
</tr>
<tr>
<td>AMT</td>
<td>1.356</td>
<td>4.051</td>
<td>7.085</td>
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<tr>
<td>AIN</td>
<td>0.863</td>
<td>1.745</td>
<td>1.227</td>
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<tr>
<td>AEX</td>
<td>0.893</td>
<td>1.797</td>
<td>1.366</td>
</tr>
<tr>
<td>AST</td>
<td>0.072</td>
<td>3.489</td>
<td>3.244</td>
</tr>
<tr>
<td>DTE</td>
<td>7.134</td>
<td>127.967</td>
<td>13.105</td>
</tr>
<tr>
<td>LEV</td>
<td>0.891</td>
<td>2.884</td>
<td>7.854</td>
</tr>
<tr>
<td>CFO</td>
<td>0.612</td>
<td>10.131</td>
<td>8.292</td>
</tr>
<tr>
<td>COM</td>
<td>1.155</td>
<td>2.333</td>
<td>2.415</td>
</tr>
<tr>
<td>VOL</td>
<td>0.516</td>
<td>1.267</td>
<td>-0.773</td>
</tr>
</tbody>
</table>

6.4.4 Autocorrelation

Autocorrelation can be defined as the correlation of a period of time possessing both future and past values, and the occurrence of autocorrelation usually leads to incorrect standard errors. We implemented the same test for autocorrelation as Ajanthan (2013) and Ntim et al. (2012) (i.e., the Durbin-Watson test). Table 6.7 presents that all the regression models results of the Durbin-Watson test range from 0.534 to 1.908 values, which indicated the absence of autocorrelation.

Table 6.7. Durbin-Watson Test (Autocorrelation)

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>ROE</th>
<th>TQ</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1.850</td>
<td>1.908</td>
<td>0.534</td>
</tr>
</tbody>
</table>
6.4.5 Linearity

Notably, a linear relationship between both independent and dependent variables is required in order for regression analysis to be utilised. Here, the residuals were plotted against the independent variable values—the same method that Alghamdi (2012) implemented. As can be seen in Figure 6.1, there was, indeed, a linear relationship between the independent and dependent variables, meaning the linearity assumption was fulfilled.

![Figure 6.1. Linearity for All Models.](image)

6.4.6 Endogeneity Problem

Considering the fact that, according to Chenhall and Moers (2007), it can result in erroneous findings in terms of hypothesis un/fulfilment, endogeneity—defined by Wooldridge (2013) as a multiple regression model’s possession of an endogenous explanatory variable that aligns with an error term—as maintained by Denis (2001), has the potential to be rather problematic when it comes to exploring the relationship between firm performance and corporate governance. Notably, omission of control variables is the primary cause of endogeneity, and it has been argued that endogeneity as a result of this can be alleviated with the careful choosing of control variables. This is because here, economic variables usually align with corporate governance (Black, Jang, & Kim, 2006). Notably, according to Chong and Lopez (2007), the omission of economic variables that influence firm performance and corporate governance can result in the erroneous estimation of both firm performance and corporate governance. An example of this would be firms that have abundant chances for expansion improving their corporate governance...
with the aim of increasing their external finances, since such firms would then be likely to employ more board independent directors.

Secondly, according to Wooldridge (2013), endogeneity can also be brought about by the inaccurate measuring of variables—something that frequently happens in corporate governance studies using indexes rather than single variables. According to Baker and Anderson (2010), this could be due to the fact that such a single variable could possibly have a smaller measured value than that of the index. Notably, according to Ntim et al. (2012) and Jo and Harjoto (2011), simultaneity is caused by at least one explanatory variable being established by the dependent variables at the same time, and, in the context of the relationship between firm performance and corporate governance mechanisms, Schultz, Tan, and Walsh (2010) provide the example that control characteristics may be established at the same time as corporate governance mechanisms. To go back to endogeneity, it is a pressing issue that none of the current literature appears to tackle the fact that endogeneity tends to incur biased findings—and it is in order to do so that the current research has implemented the Hausman Test, which, according to Ozili and Outa (2019), Neifar and Utz (2019), Elamer et al. (2019), Alzeban (2018), and Al-Shaer et al. (2017), indicates whether the random-effects regression or the fixed effects regression model would be better suited to the research at hand. As is displayed in Table 6.8, the Hausman Test showed there to be no endogeneity-driven bias in the models, since the independent variables were exogenous; furthermore, the fixed effects regression model was shown to be the most appropriate, and the $TQ$ and $ROE$ proxies to be significant, while $ROA$ was not and was thus better measured with the random-effects regression model. All of these findings enhance the strength and reliability of the results of this research, since $ROA$ indicated endogeneity, and for this analysis, robust regression was selected.

Table 6.8. Hausman Tests (Endogeneity)

<table>
<thead>
<tr>
<th></th>
<th>$\text{ROA}$</th>
<th>$\text{ROE}$</th>
<th>$\text{TQ}$</th>
</tr>
</thead>
<tbody>
<tr>
<td>$Ch^2(1)$</td>
<td>13.090</td>
<td>141.650</td>
<td>178.850</td>
</tr>
<tr>
<td>Prob &gt; $\chi^2$</td>
<td>0.519</td>
<td>0.000</td>
<td>0.000</td>
</tr>
</tbody>
</table>

### 6.4.7 Outliers

Using outlier tests, OLS assumptions, and mean and standard deviation, our $ROE$ and $ROA$ models indicated there to be an expected 68 outliers (i.e., a standard deviation
greater than 3, and things that should be deleted from analysis) for ROE and 31 outliers for ROA, considering it was a standard distribution pattern. Indeed, it was apparent that all of these outliers needed to be taken away so as to ensure a linear distribution. Meanwhile, regression analysis was also conducted both with and without the presence of outliers, the results of which showcase there to be no significant positive changes in the model, with the $R^2$ and F-value reducing. Keeping in mind that these outliers are real numbers, Hoaglin and Iglewicz’s (1987) OLS assumptions will still be implemented here.

### 6.4.8 Multivariate Analysis

Table 6.9 provides the estimated coefficients, t-statistics, significances, and standard errors of the three robust regression models, each specifying an alternate measure of firm performance (ROA, ROE, and TQ). For comparison purposes, OLS, GLS, and fixed effects regression estimates are provided for the same models (see Appendix 2). Meanwhile, the primary differences have some additional significant coefficients, but the values of $R^2$ are marginally less in GLS and fixed effects regressions (see Table 6.9 and Appendix 2). As shown, all the models in Table 6.9 were highly significant overall, and all rejected the null hypothesis that the slope coefficients were jointly zero at the .01 level.

In terms of goodness-of-fit, the models explain between 26.2% (ROA) and 29.1% (TQ) of the variation in performance.

**Table 6.9. Robust Regression Estimates**

<table>
<thead>
<tr>
<th></th>
<th>ROA Coef.</th>
<th>ROA Std. Err.</th>
<th>ROA T.stat/Sig</th>
<th>ROE Coef.</th>
<th>ROE Std. Err.</th>
<th>ROE T.stat/Sig</th>
<th>TQ Coef.</th>
<th>TQ Std. Err.</th>
<th>TQ T.stat/Sig</th>
</tr>
</thead>
<tbody>
<tr>
<td>BSZ</td>
<td>-0.036</td>
<td>0.311</td>
<td>-0.120</td>
<td>-0.451</td>
<td>0.538</td>
<td>-0.840</td>
<td>0.079</td>
<td>0.018</td>
<td>4.380***</td>
</tr>
<tr>
<td>BMT</td>
<td>-0.022</td>
<td>0.158</td>
<td>-0.140</td>
<td>-0.312</td>
<td>0.335</td>
<td>-0.930</td>
<td>0.015</td>
<td>0.010</td>
<td>1.500</td>
</tr>
<tr>
<td>BIN</td>
<td>3.408</td>
<td>0.928</td>
<td>3.670***</td>
<td>7.985</td>
<td>1.726</td>
<td>4.630***</td>
<td>0.287</td>
<td>0.095</td>
<td>3.010***</td>
</tr>
<tr>
<td>BOU</td>
<td>-5.951</td>
<td>2.317</td>
<td>-2.570**</td>
<td>-7.411</td>
<td>4.310</td>
<td>-1.720</td>
<td>0.317</td>
<td>0.140</td>
<td>2.270**</td>
</tr>
<tr>
<td>ASZ</td>
<td>-0.075</td>
<td>0.652</td>
<td>-0.120</td>
<td>2.290</td>
<td>1.480</td>
<td>1.550</td>
<td>-0.089</td>
<td>0.038</td>
<td>-2.350**</td>
</tr>
<tr>
<td>AMT</td>
<td>-0.422</td>
<td>0.457</td>
<td>-0.920</td>
<td>-0.767</td>
<td>1.002</td>
<td>-0.770</td>
<td>-0.015</td>
<td>0.025</td>
<td>-0.630</td>
</tr>
<tr>
<td>AIN</td>
<td>1.673</td>
<td>1.518</td>
<td>1.100</td>
<td>-2.238</td>
<td>2.760</td>
<td>-0.810</td>
<td>0.134</td>
<td>0.122</td>
<td>1.100</td>
</tr>
<tr>
<td>AEX</td>
<td>0.985</td>
<td>1.389</td>
<td>0.710</td>
<td>0.371</td>
<td>2.871</td>
<td>0.130</td>
<td>0.214</td>
<td>0.081</td>
<td>2.660***</td>
</tr>
</tbody>
</table>

Turning first to the estimated t-statistics for the variables describing the characteristics of the boards of directors, board size (BSZ) was statistically significant and positive in the TQ model and insignificant in the ROA and ROE models. While a significant amount of...
variation across all the models is indicated in the dependent variable by the adjusted $R^2$, the F-statistic is statistically significant. As aligns with Setia, Tanewski, and Skully’s (2009), Yawson’s (2006), and Dalton et al.’s (1998) results, the $TQ$ regression analysis shows a limited positive relationship between firm performance and board size, while $ROE$ and $ROA$ as proxies yielded no positive relationship between these two factors. Furthermore, as was stated by Goodstein et al. (1994) and Pearce and Zahra (1992), resource-dependency theory states that a larger board automatically means more resources, and, thus, firm opportunities and performance. Such a notion aligning with those of previous studies documenting that there was a positive relationship between firm performance ($TQ$) and board size, Al-Saidi (2020) and Al-Matari et al. (2012a) point out that the positive relationship between these two factors is likely because of the importance the Kuwaiti people place on personal relationships in the business context. Further, as explained by Setia et al. (2009) and Dalton et al. (1998), the insignificant relationship found between firm performance ($ROA$) and board size could be attributed to the fact that stewardship theory and resource-dependency theory both maintain that a positive relationship can only develop when a varied range of knowledge and experience is present in a given board, a lack of this leading to an insignificant relationship. This is further developed by Pratheepkanth, Hettihewa, and Wright’s (2015), Al-Matari et al.’s (2012a) and Matari et al.’s (2012c) findings, whose conclusion that there was no significant relationship between these two factors was attributed to independent directors reducing the opportunities that would normally come with a large board.

The results for the number of board meetings ($BMT$) in all model samples are not significant (see Table 6.9). These results are contradicted with H2, which stated that the higher number of meetings positively related to firm performance in Kuwaiti industrial and services firms. These results are not surprising, because the Kuwaiti industrial and services firms do not comply with corporate governance codes related to minimum numbers of meetings during the year, which is zero in several firms (see Table 6.2). The results of this study are, however, consistent with those of Uzun et al. (2004), who found there to be no relationship between board meetings and firm performance.

The regression coefficients for board independence show positive and significant effects between $BIN$ and all firm performance proxies $ROA$ (3.670), $ROE$ (4.630), and $TQ$ (3.010) at level 1% (see Table 6.9), which is consistent with previous studies (i.e., Alipour et al., 2019; Kavitha et al., 2019; Tosun & Senbet, 2020). However, it is not consistent with
studies conducted in Kuwait, whereby Al-Saidi (2020) found a negative relationship between board independence and firm performance (particularly TQ). This contradiction in results could refer to the differences in sample size and the method of calculating the TQ ratio.

For the BOU, Table 6.9 above shows that board outsiders are negatively and significantly related to ROA and ROE in Kuwaiti industrial and services firms (-2.570 at level 5%, -1.720 at level 10% respectively), these results indeed being consistent with those of prior literature (e.g., Agrawal & Knoeber, 1996; Bozec, 2005; Laing & Weir, 1999; Yermack, 1996;). On the other hand, TQ models are positively affected by BOU, these results being consistent with those of a large number of studies in developed and developing countries (e.g., Adams & Jiang, 2016; Al-Matari et al., 2012a; Al-Matari, 2014b; Arosa, et al, 2010; Pombo & Gutiérrez, 2011). The difference in these results could refer to the formula structures of the firm performance proxies, ROA and ROE being in the same group of firm evolution. Overall, there is moderate support for H1 (a positive relationship between board size and firm performance) and no support for H2 (a positive relationship between the number of board meetings and firm performance). There is also moderate support for H3 and H4 (positive relationships between board independence and the number of board outsiders and firm performance).

Turning now to the estimated coefficients for the audit committee characteristics, these generally had much less impact on firm performance, regardless of measurement. The regression coefficients for ASZ show a negative and significant effect on firm performance TQ (-2.350) at level 1% (see Table 6.9), which is consistent with the findings of previous studies (i.e., Al-Matari et al., 2012a; Bozec, 2005; Hsu & Petchsakulwong, 2010; Moilah & Talukdar, 2007). On the other hand, ROA and ROE have no relationship with ASZ, these results being consistent with those from prior studies (i.e., Al-Matari et al., 2014b; Mak & Kusnadi, 2005). Accordingly, H5 (a positive relationship between audit committee size and firm performance in Kuwaiti industrial and services firms) is not fulfilled, potentially because of the weakness of complaining with corporate governance code, although the audit committee board has the minimum number of members, whereas several firms in Kuwait do not have the minimum number (see ASZ minimum size in Table 6.2 that indicated zero value).

As for AMT, Table 6.9 shows there to be no relationship between AMT and firm performance in Kuwaiti firms, which is consistent with the results of other studies (e.g.,
Al-Matari, et al., 2014b; Alzeban, 2020; Rebeiz & Salameh, 2006; Sharma et al., 2009). These results could refer to several reasons; however, the weakness of complaining with corporate governance code meet with the minimum number of meetings whereas several firms in Kuwait do not have the minimum audit committee meetings (see AMT minimum meetings in Table 6.2 that indicated 0 value). This could also be due to the increased costs of holding frequent meetings, as well as the reverse in changes of decision taken in earlier meetings. Therefore, H6 is not supported.

In regards to the regression coefficients for audit committee independence (AIN), Table 6.9 shows no relationship between AIN and firm performance in Kuwaiti firms. These results are consistent with Kajola (2008) and Cotter and Silvester (2003), and are also not surprising, given the weakness of audit committee member independence in Kuwaiti industrial and services firms (see the AIN average in Table 6.2). Accordingly, H7 is not supported.

Prior literature states that high audit committee expertise leads to the improvement of firm performance (Chen & Komal, 2018; Lee & Park, 2019), and, indeed, this suggestion is consistent with our postulation that audit committee expertise positively relates to firm performance in Kuwaiti industrial and services firms. The results in Table 6.9 show that H8 is partially supported, whereas AEX was seen to be positively related to TQ (2.660 at level 1%). In contrast, ROA and ROE have a positive but insignificant relationship with AEX, which is consistent with Farhan et al.’s (2017) findings of no relationship between AEX and firm performance in UAE. The potential reason for these results could be the weakness of the existing audit committee expertise in Kuwaiti industrial and services firms (see the AEX average in Table 6.2).

Finally, the impact of the control variables on firm performance was examined and measured, and, as expected, firm performance positively and significantly related to firm size, except for TQ. Furthermore, DET negatively and insignificantly related to firm performance, except TQ, and LEV’s results (Table 6.9) are consistent with those of the prior literature that maintains there to be a negative relationship between LEV and firm performance (ROA is -2.350, ROE insignificant -0.240, and -5.130 for TQ). Meanwhile, cash flow improved performance, as measured by ROA, ROE, and TQ, since all the model samples were found to be positively and significantly related to CFO. Lastly, none of the corporate governance code variables in either the voluntary or compulsory regimes were significant, suggesting that there had been no additional benefit to firm performance via
corporate governance over that implied by the changes to the boards of directors and audit committees.

6.5 Conclusion

This study examined the relationship between the characteristics of boards of directors and audit committees as proxies for the quality for corporate governance and firm performance, as variously measured for Kuwaiti industrial and services firms over the period from 2010 to 2017. The selected period was particularly interesting, since it corresponded with the staggered implementation of Kuwait’s new corporate governance code and guidelines. The expectation here was that these would significantly improve corporate governance in the country, and, with it, listed firm performance.

The results with respect to the qualities of the board of directors (which were measured using board size, the number of board meetings, and the share of independent and outside directors on the board) were somewhat mixed: board size positively related to firm performance, as expected, but only in relation to $TQ$, while in contrast, the proportion of independent board members was not at all related to the firm performance models. Meanwhile, the number of board meetings related to all firm performance models, and the proportion of board outsiders only to $TQ$. Overall, board qualities jointly and significantly determined firm performance, with this best reflected in the returns on $TQ$.

As for audit committee characteristics, only audit committee expertise related to firm performance. Further, the sign on the estimated coefficient for committee size did not correspond with the hypothesis of a positive relationship with firm performance. One possible reason for this is that too large a committee is ungainly and unable to effectively perform its supervision and risk assessment role, or, alternatively, it could be that the proxies used for the quality of the audit committee in relation to good corporate governance, while well established in the literature, do not actually do a very good job of outlining firm performance. An alternative to this is that while audit committees are a key part of the firm’s good governance in terms of accountability, compliance, and risk management, they simply may not be as influential at the margin (as far as firm performance is concerned) as the board of directors that selects them.

A challenging feature of the results is that, apart from their impact on the several board and audit committee qualities, the different corporate governance code and guideline regimes through which these firms progressed during the sample period had no significant
impact on firm performance. Moreover, it would appear that Kuwait’s corporate governance code and guidelines (at first voluntary and then compulsory) have had the most effect on audit committees, but little measured effect on firm performance. One possibility for this is that Kuwait’s corporate governance code and guidelines merely codified corporate governance practices that were mostly or increasingly in place among its boards, and, while invoking substantial change to audit committees, involved little change to firm performance. It is also likely that firms began to make the necessary changes in anticipation of these changes as a means of strengthening their organisational legitimacy by aligning their corporate governance practices with the expectations of the investor community.

The number of listed industrial and services firms in the sample was relatively stable until 2017, when it fell by 17 firms (some 26%). One possible reason for that is that the firms that delisted did so in consideration of the new corporate governance code and guidelines becoming compulsory, as they may not have been able or willing to bring about the changes involved. This suggests that the reforms not only marginally improved the governance and performance of firms that continued listing on the KSE, but also provided an incentive for firms with poor corporate governance and/or firm performance to leave the market. Either way, the quality of corporate governance and the level of firm performance in the KSE improved noticeably. However, further research would still be required in order to investigate whether self-selection was more than a possibility.

This study revealed several practical and social implications: the recent corporate governance code and guideline reforms have exerted a mixed impact on firm performance, with audit committees being the most influenced. However, recent reforms mostly involved changes to the boards of directors, and so it could be suggested that nonmarket reforms may have been unneeded given existing market pressure on listed firms and firms anticipating regulatory change. In addition, Kuwait’s corporate governance reforms likely codified corporate governance practices already in place among many of its firms in pursuit of organisational legitimacy, and, while invoking substantial change to audit committees, ultimately involved little change to firm performance in the short term. Some firms may also have delisted in expectation of stronger corporate governance requirements. Regardless, these direct and indirect processes both improved the overall quality of listed firm corporate governance and performance in Kuwait.
There is certainly a need for more research on the proxies typically employed in assessing the governance qualities of boards and audit committees; while quantitative measures of the size, frequency of meeting, and levels of independence and outsiders (boards) or expertise (audit committees) are associated with good corporate governance and therefore firm performance, another possibility is the qualitative insights obtained from surveys and interviews of board members (including those on audit committees, firm management, and regulators). At the very least, this would further ensure the robustness of these and similar findings.
Chapter 7: Qualitative Insights Into Corporate Governance Reform, Management Decision-Making, and Accounting Performance: Semi-Structured Interview Evidence

This chapter comprises a paper prepared as a working paper and submitted for publication in a peer-reviewed journal as follows:

Alajmi, A. and Worthington, A.C. “Qualitative Insights Into Corporate Governance Reform, Firm management, Organisational Change and Accounting Performance: Semi-structured Interview Evidence”, under editorial review at Qualitative Research in Accounting and Management.

This paper aims to enhance understanding of the relations between corporate governance reform, management decision-making, and firm accounting performance in Kuwait by focusing on the role of important, but difficult-to-measure quantitative factors, including cultural, religious, tribal, and political circumstances. Data were collected using semi-structured interviews and analysed using coding and quoting approaches. The coding approach categorises the responses into themes and sub-themes and the quoting approach adds depth to this categorisation. The findings show that a range of external cultural factors, including religion, politics, and Kuwait’s tribal system, along with economic and financial circumstances and accounting standards, influence the corporate governance – firm performance relationship in Kuwait. The findings are of value to domestic and international investors gauging investment risk, firm managers operating within a growing and developing but still traditional market, and regulators seeking ongoing improvements in corporate governance, including disclosure, openness, and transparency.
STATEMENT OF CONTRIBUTION TO CO-AUTHORED PUBLISHED PAPER

- The candidate’s contribution to this paper consisted of researching and writing the literature review, formulating and conducting the methodology, analysing and writing up the results, and preparing and formatting the text, tables, and figures.
- Andrew Worthington’s contribution to the paper involved guiding the research design and editing.

7.1 Introduction

Corporate governance—the framework that defines the relationships between shareholders, management, the board of directors, and other stakeholders—lies at the heart of how firms operate and perform. Good corporate governance protects shareholder rights, enhances disclosure, openness, and transparency, facilitates the effective functioning of boards, and provides an efficient legal and regulatory enforcement framework. Good corporate governance also encourages shareholder participation, provides incentives for the board and management to work in the interests of the firm and its shareholders, and makes them accountable for their actions. Finally, good corporate governance ensures that firms make decisions on an ethical and responsible basis and that all risks to the company are appropriately recognised and managed (Azim, 2012). Ultimately, by better managing the fundamental agency and stakeholder relationships in the firm, these come together to enhance corporate performance.

There is considerable uncertainty as to which aspects of corporate governance are most beneficial regarding the corporate governance – firm performance relationship. Some studies have addressed the impact of different shareholder groups (including family, institutional, and government ownership) on the quality of corporate governance, and hence, performance (Sakawa & Watanabel, 2020). Others have considered the impact of important corporate governance mechanisms, including the composition of the board of directors and audit committees. Nearly all have employed quantitative methods, especially regression analysis, to measure the association between corporate governance variables and firm performance as variously defined, including market measures such as stock returns, accounting measures such as return on assets and equity, and hybrid measures combining both, such as Tobin’s Q (Cao, Cumming, & Zhou, 2020).

Unfortunately, quantitative methods suffer some limitations when exploring the relationship between corporate governance and firm performance. First, corporate
governance is first and foremost a legal framework, and is often difficult to quantitatively proxy the nuances found in complex legislation (Sakawa & Watanabel, 2020). This explains the readiness of many capital markets, accounting, and finance studies to only consider the most easily identified aspects of corporate governance, such as the size of boards, the number of board meetings, and the percentage holdings of particular shareholder groups. For the same reason, they likely ignore aspects of corporate governance that seemingly defy parametrisation, including immeasurable contextual features such as culture, religion, and politics.

Second, the focus on good corporate governance has developed unevenly throughout the world, and in many places where it is now being implemented, financial statements and other information necessary for quantitative analysis may be incomplete and of short duration (Cao et al., 2020). This is a problem in that the developing market contexts where corporate governance frameworks, principles, and practices are rapidly changing is often of interest.

Both of them are applicable to the chosen context of Kuwait for this study, as it is a small but influential economy in the Arabian Gulf. For much of its recent business history, corporate governance practices in Kuwait have not kept pace with the growth of its companies and equity market as a whole. In fact, Kuwait did not implement its first corporate governance code and guidelines to address some of its longstanding corporate governance failings until 2013. These included excessively large block and pyramid shareholdings, unusually complex corporate structures, poor disclosure and transparency practices, and the concentration of and interlocking directorships (Pillai & Al-Malkawi, 2018).

Firms listed on the Kuwait Stock Exchange (KSE) are now subject to two sets of regulations: capital markets authority laws used to regulate the behaviour of market participants and firm (so-called ministry) laws. Together, these laws impose many corporate governance articles and provisions newly obliging all listed firms to make necessary changes to their bylaws and internal policies. For boards, they include board size and composition, the required separation of the board chair and chief executive officer, regulations governing executive and non-executive members, and a requirement for independent directors. For audit committees, they include committee size and meetings, the requirement for members to hold professional certification, the designation
of roles not permitted to meet with internal and external auditors, and a requirement for independent members.

Lastly, for shareholders they include basic shareholder rights, including to meetings, voting and dividends, disclosures of ownership and declaration of direct and indirect relations between the firm and major shareholders, and compliance, disclosure and transparency requirements for other stakeholders. Nearly as interestingly, the implementation of these requirements was staggered. Prior to 2013, there were no corporate governance code or guidelines in Kuwait; from then until 2015 there was only voluntary compliance; and from 2016 onwards, there was compulsory compliance.

Qualitative analysis is well suited to this situation (Charmaz, 2006; Sandelowski, 1995). The approach chosen for this study consists of semi-structured interviews with general and financial managers and board chairpersons in a sample of Kuwaiti listed firms, with a focus on immeasurable or difficult-to-measure variables that affect the nature of the relationship between corporate governance and firm performance in Kuwait, such as politics, culture (especially Kuwait’s strong tribal system), and religion. The effects of different approaches to the use of information technology (IT) within company accounting systems and the effects of politically sensitive matters, such as foreign, local, institutional, and family ownership, are also considered.

Several areas of relevance to the corporate governance – firm performance relationship were also discussed during the interviews, including the role of Kuwait’s Capital Markets Authority and corporate governance reform, the restive factors affecting corporate governance and firm performance (e.g., culture, politics, religion, and the tribal system), and shareholders’ and managers’ incentives to increase firm profit. Likewise, the country’s adoption of International Financial Reporting Standards (IFRS) and its relationship to corporate governance in Kuwait, financial crises and firm performance, accounting systems in Kuwaiti firms, boards of directors, audit committee roles, and firm performance, and ownership structure and firm performance were also considered. This is a wide-ranging inquiry into extensive corporate governance reform by any measure.

The findings of this study are potentially useful to investors, who can use the results to manage the potential risks that face Kuwaiti firms now and in the future, including not only economic, financial, operational, and competition risk, but also compliance, security and fraud, and reputational risk. Similarly, the results may provide some comfort to senior managers struggling to deal with cultural factors and the tribal system in Kuwait and its
impact on corporate governance and firm performance, matters unexplained by existing quantitative analysis. Lastly, the results may help inform ongoing efforts by legislators and regulators in continuously improving corporate governance in Kuwait, elsewhere in the Middle East, and in developing economies more generally.

The remainder of the paper is structured as follows. Section 7.2 discusses the sampling of interviewees, the interview questions, and the analytical technique applied to the interviewees’ responses. Sections 7.3, 7.4, 7.5, and 7.6 analyse the institutional and regulatory, sociological, external accounting and financial, and internal managerial and accounting factors arising from the interviews, respectively. Section 7.7 provides the conclusion.

7.2 Methodology

7.2.1 Interview Sample

Interviews were concluded with 14 managers, comprising six general managers, five financial managers, and three board chairpersons from nine companies. Firms from all 62 Kuwaiti industrial and services firms listed on the KSE were randomly selected, but with three purposively chosen across three performance categories: high, moderate, and low firm accounting performance. Performance was defined according to an equal weighting of common accounting measures of firm performance, namely, return-on-assets (ROA), return-on-equity (ROE), and Tobin’s Q (TQ). However, financial firms (i.e., banking and insurance firms) have been removed from our sample, as these firms have different rules and regulations and financial accounting standards. Accordingly, the inclusion of banking and insurance firms in the study sample could possibly misrepresent the study results.

For the qualitative aspects of the study, the relevant ethics underpinning the study’s transparency and management were the primary focus. Here, Griffith University’s Human Investigation Team and consultants were of utmost importance, and were invaluable to the study’s ethical conduct. Indeed, all ethical considerations were dealt with carefully and thoroughly to ensure a fully valid, principled investigation, and this could not have been achieved without Griffith University’s resources.

Appendix 3 provides the full details of the ethical clearance for the study (protocol number GU Ref No: 2017/903). Such clearance was required due to the rules and regulations of human research within Griffith University. Furthermore, it is of the highest importance that all data analysis, handling, noting, and broadcasting is undertaken with
utmost transparency and veracity—factors that cannot be separated from the study’s very essence to ensure wholly valid and representative research.

Table 7.1 summarises the characteristics of the interviewees, including education, qualifications, and experience in the firm. As shown, most of the interviews were with general managers (43%), followed by financial managers (36%), and board chairpersons (21%). Of these, 57% held bachelor’s, master’s, or doctoral degrees in accounting, 22% in business, 14% in finance, and 7% in economics. Only a single interviewee held a CPA qualification. In terms of experience, 50% of interviewees had long periods of work experience in their current firm (>10 years), 36% had medium experience (5–9 years) and 24% had experience of less than five years. Together, these statistics suggest that the interviewees were sufficiently well qualified and experienced to provide in-depth insights about the corporate governance–firm performance relationship in contemporary Kuwaiti firms.

Table 7.1. Interviewees

<table>
<thead>
<tr>
<th>Firm performance</th>
<th>Firm</th>
<th>Interviewee</th>
<th>Position</th>
<th>Academic qualification</th>
<th>Professional qualification</th>
<th>Years of firm experience</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>1</td>
<td>1</td>
<td>FM</td>
<td>BA Accounting</td>
<td>–</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>3</td>
<td>GM</td>
<td>BA Business</td>
<td>–</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>3</td>
<td>4</td>
<td>D</td>
<td>BA Business</td>
<td>–</td>
<td>17</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>C/FM</td>
<td></td>
<td>BA Finance</td>
<td>–</td>
<td>4</td>
</tr>
<tr>
<td>Moderate</td>
<td>7</td>
<td>11</td>
<td>FM</td>
<td>BA Accounting</td>
<td>–</td>
<td>12</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>13</td>
<td>GM</td>
<td>Accounting</td>
<td>–</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>9</td>
<td>14</td>
<td>D/C</td>
<td>BA Economics</td>
<td>CPA</td>
<td>9</td>
</tr>
<tr>
<td>Low</td>
<td>4</td>
<td>6</td>
<td>D</td>
<td>PhD Accounting</td>
<td>–</td>
<td>13</td>
</tr>
<tr>
<td></td>
<td>7</td>
<td>C/GM</td>
<td></td>
<td>BA Accounting</td>
<td>–</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>8</td>
<td>8</td>
<td></td>
<td>MSc</td>
<td>–</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>5</td>
<td>9</td>
<td>FM</td>
<td>Accounting</td>
<td>–</td>
<td>7</td>
</tr>
<tr>
<td></td>
<td>6</td>
<td>10</td>
<td>GM</td>
<td>BA Accounting</td>
<td>–</td>
<td>5</td>
</tr>
</tbody>
</table>

Note: FM – Financial manager, GM – General Manager, D – Director, C – Chairperson.

7.2.2 Interview Questions

Semi-structured interviews are a data-gathering method consisting of oral communication between the researcher and the interviewees, normally used in investigation strategies, in exploratory methods, and in social studies, including accounting. A variety of interviewing methods are available, ranging from fully unstructured (no questions and
open responses) to fully structured (set questions and closed responses) (Bauman et al, 2002). The semi-structured approach employed in this study involved the participant responding to guiding questions in an open fashion, which typically yields more accurate and in-depth information related directly to the phenomena under investigation (Opdenakker, 2006). Here the interviewer posed questions in the form of an interview schedule, standardised to ensure that the differences between interviews were minimised. However, the sequence of the questions could be changed at the interviewer’s discretion, with follow-up questions available for some significant responses (Bryman & Bell, 2015).

Table 7.2 lists the guiding questions and the interview schedule. Each interview consisted of two parts, as is the norm (Mojtahed et al., 2014). The first part consisted of basic interviewee information, including the interviewee’s position and role in the firm, experience, education, and gender. This section focused on providing information that guided the researcher to determine the interviewees’ ability to provide the proper information, in addition to ensuring that interviewees were qualified to increase the validity and reliability of research. The second part comprised how/what/why questions concerning perceptions of internal and external factors affecting corporate governance and its outcomes. The interviews ranged in length from 35 to 75 minutes.

Table 7.2. Guiding Questions

<table>
<thead>
<tr>
<th>About You</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>— What is your position and role in this firm?</td>
<td></td>
</tr>
<tr>
<td>— What is your previous work experience?</td>
<td></td>
</tr>
<tr>
<td>— What are your academic qualifications?</td>
<td></td>
</tr>
<tr>
<td>— Do you have any professional qualifications?</td>
<td></td>
</tr>
<tr>
<td>About Your Firm</td>
<td></td>
</tr>
<tr>
<td>— How would you describe the development of the corporate governance code in Kuwait?</td>
<td></td>
</tr>
<tr>
<td>— How would you describe the governance structure in your firm?</td>
<td></td>
</tr>
<tr>
<td>— Do you believe the capital market authority (CMA) effects the development of corporate governance in Kuwait? Give an example and how you believe this role has changed over time.</td>
<td></td>
</tr>
<tr>
<td>— What factors do you consider could potentially affect the relation between the following and firm performance:</td>
<td></td>
</tr>
<tr>
<td>— The board of directors?</td>
<td></td>
</tr>
<tr>
<td>— The audit committee?</td>
<td></td>
</tr>
<tr>
<td>— The makeup of shareholders?</td>
<td></td>
</tr>
<tr>
<td>— The conduct of internal audits?</td>
<td></td>
</tr>
<tr>
<td>— What cultural factors do you consider might affect your firm (including tribal system, education, experience, religion)?</td>
<td></td>
</tr>
<tr>
<td>— Do you believe politics and economics affect the performance of your firm? How?</td>
<td></td>
</tr>
<tr>
<td>— Do you believe shareholders and manager incentives affect the performance of your firm? How?</td>
<td></td>
</tr>
<tr>
<td>— Do you believe that the adoption of International Financial Reporting Standards (IFRS) has affected corporate governance and firm performance in Kuwait? How?</td>
<td></td>
</tr>
<tr>
<td>— Do you believe that financial crises affect the performance of your firm? How?</td>
<td></td>
</tr>
<tr>
<td>— Which type of accounting system does your firm use? Give an example.</td>
<td></td>
</tr>
<tr>
<td>— Do you believe that the type of ownership affects your performance of your firm? How?</td>
<td></td>
</tr>
</tbody>
</table>
--- Can you identify the board of directors and audit committee members for your firm?
--- What do you know about the roles of the board of directors and the audit committee?
--- Is the CEO and chair of the board of directors of your firm the same person?
--- What do you see as the main obstacles your firm faces in achieving high performance?

7.2.3 Analytical Approach

Two methods were used to analyse the recorded, translated (from Arabic to English), and transcribed interviews: the coding approach and the quoting approach (Engkizar et al., 2018; Sams, 2010). In support, Brown and Brignall (2007) argued that the use of more than one method in analysing the same dataset leads to complementary results, which in turn improves the validity and reliability of any results. The coding approach was used to thematically categorise and organise the interview information and the quoting approach was used to provide depth and perspective to this coding.

Preceding the quoting approach—which was largely employed so as to support and improve the key sub-themes and themes present here (please see Tables 7.3 to 7.6)—this investigation opened with the employment of the coding approach, with the key objective of creating a robust framework. While this approach has the potential to reduce the validity present within the research, semi-structured, open-ended interviews are usually employed because they are able to create an environment conducive to open and honest conversation—something of high importance when it comes to interviews concerning taboo subject matter (Yun et al., 2020).

The first stage of code creation was the transcribing of all responses provided during the interviews. This allowed for complete familiarisation with the data, an essential step. All collected information was then outlined in terms of relevance to the study, and categorised according to whether this fell under the key ‘themes’ or ‘sub-themes’. This was done manually rather than using qualitative data analysis software such as NVivo.

Table 7.3 sums the number of references made to each sub-theme for each performance category, ranking them in descending order of the number of references. The final column in Table 7.3 identifies the performance category (high, moderate, low) that ranks each sub-theme highest. The quoting approach was then used for the initial code in each sub-theme to reveal positive and negative interviewee opinions concerning the nature of the relationship between corporate governance and firm performance—something that enables these decision-makers to enhance their decisions in their firms.
### Table 7.3. Sub-theme Reference Summary

<table>
<thead>
<tr>
<th>Sub-theme</th>
<th>High</th>
<th></th>
<th>Moderate</th>
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<th>Low</th>
<th></th>
<th>Relatively highly ranked</th>
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<td>4</td>
<td>7</td>
<td>7</td>
<td>9</td>
<td>High</td>
</tr>
<tr>
<td>The restive factors (cultural factors)</td>
<td>26</td>
<td>3</td>
<td>13</td>
<td>1</td>
<td>27</td>
<td>1</td>
<td>Moderate/low</td>
</tr>
<tr>
<td>The restive factors (religion)</td>
<td>14</td>
<td>8</td>
<td>6</td>
<td>6</td>
<td>13</td>
<td>6</td>
<td>Moderate/low</td>
</tr>
<tr>
<td>The restive factors (political issues)</td>
<td>18</td>
<td>5</td>
<td>13</td>
<td>1</td>
<td>12</td>
<td>7</td>
<td>Moderate</td>
</tr>
<tr>
<td>The restive factors (tribal system)</td>
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<td>9</td>
<td>2</td>
<td>10</td>
<td>10</td>
<td>8</td>
<td>Low</td>
</tr>
<tr>
<td>Other modifiers (IFRS adoption)</td>
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<td>2</td>
<td>3</td>
<td>9</td>
<td>19</td>
<td>2</td>
<td>High/low</td>
</tr>
<tr>
<td>Other modifiers (financial crisis)</td>
<td>22</td>
<td>4</td>
<td>9</td>
<td>5</td>
<td>14</td>
<td>5</td>
<td>High</td>
</tr>
<tr>
<td>Manager incentives and remuneration</td>
<td>17</td>
<td>7</td>
<td>13</td>
<td>1</td>
<td>19</td>
<td>2</td>
<td>Moderate</td>
</tr>
<tr>
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<td>11</td>
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<td>10</td>
<td>Moderate</td>
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<td>142</td>
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</tr>
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</table>

Tables 7.4–7.6 list all ten sub-themes identified for each performance category (high, moderate, and low), all of which revolved around the central theme of corporate governance and firm performance, including the corporate governance code, the Kuwait Capital Markets Authority Law (CMAL) and Kuwait Companies’ Law (KCL), restive factors, other modifiers, manager incentives and remuneration, and accounting systems.
Table 7.4. Final List of Codes, References, and Sub-themes (High Performance)

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<tr>
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<th>Sub-theme</th>
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<td>Governance Code</td>
</tr>
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<td>Corporate Governance Code voluntary</td>
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<td></td>
</tr>
<tr>
<td>Developing IFRS rules</td>
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<td>Capital Markets</td>
</tr>
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<td>Authority</td>
</tr>
<tr>
<td>Issuing new laws</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Top market</td>
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<td></td>
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<td>Cultural factors</td>
<td>7</td>
<td>The restive factors</td>
</tr>
<tr>
<td>Understanding international culture</td>
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<td>(cultural factors)</td>
</tr>
<tr>
<td>Language</td>
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<td></td>
</tr>
<tr>
<td>Mentalities</td>
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<td></td>
</tr>
<tr>
<td>Education</td>
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</tr>
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<td>Religion impact</td>
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<td>The restive factors</td>
</tr>
<tr>
<td>Straightforward person</td>
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<td>(religion)</td>
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<td>Religion and lifestyle</td>
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<tr>
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</tr>
<tr>
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<tr>
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<td>The restive factors</td>
</tr>
<tr>
<td>Political connections</td>
<td>5</td>
<td>(political issues)</td>
</tr>
<tr>
<td>Revolutions</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>Political corruption</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>Tribal power to hire employees</td>
<td>7</td>
<td>The restive factors</td>
</tr>
<tr>
<td>Favouritism</td>
<td>3</td>
<td>(tribal system)</td>
</tr>
<tr>
<td>Starting IFRS adoption in 2016</td>
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<tr>
<td>Before IFRS adopting</td>
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<td></td>
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<td>IFRS adoption in developing countries</td>
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<td></td>
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<tr>
<td>IFRS adoption advantages</td>
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<td>Financial crisis 2008</td>
<td>7</td>
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<td>Fake firms</td>
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</tr>
<tr>
<td>Signing new agreements</td>
<td>2</td>
<td>Other modifiers</td>
</tr>
<tr>
<td>Restricting loan processes</td>
<td>3</td>
<td>(financial crisis)</td>
</tr>
<tr>
<td>Growing firms</td>
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<tr>
<td>Customers decreasing</td>
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<td>Shortage income</td>
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<td>Board of directors rules</td>
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<td>Personal motivations</td>
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</tr>
<tr>
<td>Shareholders motivations and targets</td>
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<td>and remuneration</td>
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<td>Bonuses and compensations</td>
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<tr>
<td>Positive incentive impact</td>
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### Table 7.5. Final List of Codes, References, and Sub-themes (Moderate Performance)

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<tr>
<td>Cultural factors</td>
<td>4</td>
<td>The restive factors (cultural factors)</td>
</tr>
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<td>Networking (nepotism)</td>
<td>7</td>
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</tr>
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<td>Mentalities</td>
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</tr>
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<td>Religion impact</td>
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<td>The restive factors (religion)</td>
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<td>Religion behaviour</td>
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<td>The restive factors (religion)</td>
</tr>
<tr>
<td>Straightforward person</td>
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<td>The restive factors (religion)</td>
</tr>
<tr>
<td>Weakness political</td>
<td>2</td>
<td>The restive factors (political issues)</td>
</tr>
<tr>
<td>Political dilemma</td>
<td>7</td>
<td>The restive factors (political issues)</td>
</tr>
<tr>
<td>Political connections</td>
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<td>The restive factors (political issues)</td>
</tr>
<tr>
<td>Revolutions</td>
<td>2</td>
<td>The restive factors (political issues)</td>
</tr>
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<td>The restive factors (political issues)</td>
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<td>Favouritism</td>
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<td>Financial crisis 2008</td>
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</tr>
<tr>
<td>Growing firms</td>
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<td>Other modifiers (financial crisis)</td>
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<td>Other modifiers (financial crisis)</td>
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<td>Other modifiers (financial crisis)</td>
</tr>
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<td>Personal motivations</td>
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</tr>
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<td>Shareholders motivations and targets</td>
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</tr>
<tr>
<td>Bonuses and compensations</td>
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</tr>
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Table 7.6. Final List of Codes, References, and Sub-themes (Low Performance)

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<tr>
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7.3 Analysis of Institutional and Regulatory Factors

7.3.1 Corporate Governance Reform

As shown in the first row in Table 7.3, high-performing firms referenced corporate governance reform 73% more than moderate- and low-performing firms combined. Corporate governance reform was also ranked first for high-performing firms, but only fourth for moderate-performing firms and seventh for low-performing firms. Historically, Kuwait is a rapidly growing and developing country, particularly following the oil revolution of the 1950s, and an attractive destination for investors. After the 2008 global financial crisis, Kuwait increasingly turned to international markets, such as the UK, US, and Japan, to offset its effects, one consequence being a significant improvement in market quality. In this regard, two managers commented:

Kuwait is considered one of the most important countries that has a great economic growth since its independence in 1961 … Where the main objective of it was achieving more economic growth in order to make Kuwait to be amongst the best countries around the world … I mean from the leading countries around the world, like the UK and USA. (FM, Moderate)

Yes, our county received important consideration with our Emir [the current Emir of Kuwait, Sabah Al-Ahmad Al-Jaber Al-Sabah, sworn in on 29 January 2006] … and since our independency [sic]; Kuwait was achieving economic growth … But there were several financial crises and political issues that affect our economic growth, such as the financial crisis in 2008, the financial crisis 1997, the political issues in 1991, and the political issues from 2010 until this moment. (C, Low)

Accordingly, Kuwait employed two new laws to achieve its objectives by developing its markets and avoiding risk that arose from the financial crisis, these being the CMAL and the KCL. One interviewee stated that issuing both sets of laws supported the Kuwaiti market as follows:

I believe that issuing the CMAL and the KCL is very supportive of our country in order to achieve more development in all our industrial, financial, and services sectors … for example, by applying these two laws, a lot of development has arisen in our business life … Another example: starting applying the new corporate governance code increases the transparency in our firms and organises all the relationships between firms’ structures. (GM, Firm 2, High)
In 2010, Kuwait established the Capital Markets Authority (CMA) and the regulation of securities activities to promote the ongoing development of the Kuwaiti market. However, there were several gaps and weaknesses in its existing regulations and policies. In response, the CMA issued the New Companies’ Law of Kuwait, comprising Law No. 1 of 2016 in conjunction with its own executive regulations, collectively known as the New Companies’ Law (NCL). The main purpose of the NCL was to overcome the weaknesses and gaps in the CMAL (Bouresli & Aldeehani, 2017). In this regard, one of the interviewees stated:

Without these two laws—I mean the CMAL and the KCL, our firms defiantly will use their personal identity in order to achieve their desirable goals, which will lead to a decrease in the development in our country. (GM, Firm 2, Moderate)

In 2013, regulators in Kuwait began working to introduce a corporate governance code, leading to greater organisation and standardisation of firm structure and transactions (Al-Saidi & Al-Shammari, 2014). However, adherence to the new corporate governance code was voluntary until the end of 2015. Nonetheless, many Kuwaiti firms began to follow the new corporate governance code, as they seemed to realise that it would solve several pervasive problems in the Kuwaiti capital market, such as distinguishing between the duties and responsibilities of boards of directors and other firm structures (Alfraih & A Almutawa, 2017). One manager discussed this voluntary adoption of the corporate governance code in Kuwaiti firms and its effect on firm management:

[I]n 2013, the business life in our firms started directing to the right path once our government introduced the corporate governance code as voluntary … However, the level of our management became much better compared with the previous period. (GM, Firm 3, High)

From early 2016, the corporate governance code became compulsory for all Kuwaiti firms, and many of the interviewees linked this directly to improvement in their firm’s performance (whether financially or operationally) and transparency. Most of the interviewees agreed that the compulsory corporate governance code was a major development in their firm’s day-to-day operations and a major turning point in Kuwait’s economic and financial development.

We feel that everything in our firm business life started developing quickly after 2016, after adopting the corporate governance code as compulsory … Accountability, independently, and transparency in our firms became higher-
level compared to previous years. (GM, Firm 2, +/-ve; GM, Firm 3, High; BC, Firm 3, High; GM, Firm 3, Low)

I am so happy that we are adopting the compulsory corporate governance code … I think, easily now, we can compare our financial and operation information with developed countries. (GM, Firm 1, Low)

7.3.2 The Capital Markets Authority (CMA)

As shown in the second row in Table 7.3, high-performing firms referenced the CMA 64 percent more than moderate- and low-performing firms combined. The CMA also ranked fifth for high-performing firms, but only seventh and ninth for moderate- and low-performing firms, respectively. The CMA was created to provide regulatory oversight of Kuwait’s listed firms and to increase the growth of Kuwait’s financial markets. Its stated aims were to ensure the control of security activities based on fairness, increase the degree of transparency in financial and operational transactions, increase capital market growth, and increase the reliability and validity of financial instruments to meet those of international markets. Its stated aims also included increasing the level of investor security, decreasing the degree of security activity systemic risk, increasing the degree of disclosure to raise transparency levels within the final statements, reducing the conflicts between owners and management, and controlling the compliance levels of adopting government regulations and policies. Most of these come under Law No. 7 (CMA, 2018):

- Securities’ activities should be regulated efficiently, transparently, and fairly.
- Capital markets should be grown with the investment instruments developed and diversified in line with the best international practice. Investor protection should be improved and ensured. Systemic risks stemming from securities’ activities should be minimised. Requirements centred on complete and transparent disclosure should be obligatory to ensure fairness and transparency, and also to help to reduce conflicts of interests and the use of insider information. Compliance with, and adherence to, the rules and regulations in regard to the securities’ activities should be enhanced and improved.

In reference to this, two interviewees stated the following:

We understood these rules, but unfortunately, still, there are weaknesses in applying these rules … For example, financial instruments are determined in Kuwait, and should be followed by each firm according to the international standard (such as IFRS), but until this moment, the personality is dominated by
some firms by using different techniques in order to achieve their desirable incentives. (FM, Firm 2, Low)

If we are following the CMA rules … I think we will be on the right side, since the rules of CMA are clear and corresponded with international rules, particularly in developed markets. (FM, Firm 1, Moderate)

From the point of view of the significance of transparency and disclosures in capital markets, there have been many changes. In this regard, one of the board of directors stated:

It’s clear, from the latest changes, that the CMA, during the last three years, know the Kuwait market is looking to be one of the top markets over the world. (BC, Firm 3, High)

This belief that the various reforms have significantly improved Kuwait’s global investor ranking is also evident outside the current study (Alfraih & Almutawa, 2017):

The Kuwaiti Government is working hard to develop its economy and improve its business environment and accounting practices. In this respect, Kuwait may be said to be one of the leading countries in adopting the International Financial Reporting Standards (IFRS). In April 1990, the Ministry of Commerce and Industry (MCI) issued the Ministerial Resolution No. 18, which stated that all listed companies on the KSE should comply with the IFRS requirements. A permanent technical committee of the MCI, established by Ministerial Decree No. 75/1981, undertakes the task of approving the application of the standards and their suitability for the business environment.

Accordingly, the adoption of IFRS is one of the Kuwaiti Government’s important targets to increase the transparency and trustworthiness of Kuwaiti firms’ financial statements. Furthermore, IFRS adoption will increase the ability of Kuwaiti firms to compare their financial statements with other firms around the world (Alfraih & Almutawa, 2017). Some interviewees, likewise, spoke of the importance of IFRS adoption:

I think the adoption is important to enhance our firms’ financial statements quality to provide more reliable and in-depth information to the users, which will lead to an increase in the trust in our firms’ financial statements. (FM, Firm 1, High)
IFRS is a great step to develop our firms’ financial statement … For example, the full adoption of IFRS is more likely related to more financial statements quality. (GM, Firm 1, Low)

Kuwait has also paid more attention to the improvement, development, and integration of its corporate governance code, especially in light of the NCL introduced in 2012 and its strong emphasis on corporate governance principals. In this regard, one interviewee stated:

I believed that the introduction of the NCL in 2012 was the first step that led our country to start thinking seriously to establish an integrated corporate governance code for Kuwaiti firms … Which is what happened in early 2013. (BC, Firm 3, Moderate)

This emphasis on disclosure to achieve transparency and justice, and to avoid conflicts of interest, was a clear advantage of the new regulation as far as the interviewees were concerned:

Several issues occurred once the Kuwait government started establishing the new corporate governance code to meet the requirements of the other countries that our government signed with their contracts … I think more reliability will lead us to achieve more goals that we are looking for, such as to be amongst the developed countries within a few years. (GM, Firms 2, Low +/-)

7.4 Analysis of Sociological Factors

7.4.1 Culture

Cultural factors are among the most important external factors influencing business, not least in Kuwait. This section discusses this in depth, providing information about the cultural factors that affect Kuwaiti firms and their influence on corporate governance and firm performance. As shown in the third row in Table 7.3, high- and low-performing firms both referenced cultural factors twice as often as moderate-performing firms, but ranked first for both moderate- and low-performing firms and third for high-performing firms. To start, most of the interviewees revealed that cultural factors were one of the most important issues affecting corporate governance and firm performance in Kuwait.

Cultural factors are indirect issues that affected the firm performance and business structure … Most of our managers ignore these factors that are important, if they considered them. (BC, Firm 3, Moderate)
Networking between the people is another issue that leads to more weaknesses for firm performance. For example, hiring unqualified employees at any level is sure to lead to a lot of error and mistakes in our financial statements. (GM, Firm 3, Low)

I think that the successful managers should consider the cultural factors when they start evaluating their businesses, whether financial or operation. (FM, Firm 1, Moderate)

Once again, there is alternative existing evidence for the impact of culture on corporate governance. For example, Humphries and Whelan (2017) considered the impact of national culture on corporate governance codes across 55 countries, using published reports to collect information on corporate governance, as well as power distance, individualism, collectivism, masculinity, femininity, and uncertainty avoidance, as proxies to measure cultural factors. The interviews also illustrated the importance of culture:

Understanding international culture is very important, which will lead to reduction of the gaps in our business, particularly when we have international branches for our business … In the end, I would say that the cultural factors, whether local or international, are very important to assess business transactions. (BC, Firm 3, High)

Using a sample of Swiss firms, Volonté (2015) found that complexity sometimes made aligning cultural variation with a common corporate governance regulatory framework difficult. They found that differences in language and culture generated differences in work styles, leading to problems in implementing strategy. In this respect, the interviewees offered the following insights:

Yes, language is a link of communication between the employees … without the existence of unified language, more problems will occur … this in turn will lead to more weaknesses in evaluating the corporate governance and firm performance. (FM, Firm 2, Low)

Misunderstandings between the employees and management because of language is the main problem that we are dealing with nowadays … Since we have more than 25 nationalities here in Kuwait … From my experience, I remembered that
one employee told him to do a certain piece of work, and unfortunately, he did the work in a different way since he misunderstood me. (GM, Firm 2, Low)

For this reason, Mertzanis et al. (2019) recommended that regulatory authorities in all Middle Eastern and North African countries should directly consider cultural factors when assessing firm performance.

In terms of other factors, Osemeke and Osemeke (2017) revealed that the childhood experience of employees within a particular culture could also affect corporate governance and perceptions of the abuse of power by top management, weak legal frameworks, poor recruitment, and ineffective control, which led to weak firm performance. Guiso, Sapienza, and Zingales (2015) likewise studied how cultural factors could affect firm performance, finding that trust between managers and employees in a solid corporate governance framework led to strong firm performance, while Thanetsunthorn and Wuthisatian (2016) revealed the role of three cultural factors (community style, employee mentality, and environmental circumstances) in a range of countries. Lastly, Ntongho (2016) concluded that US firms often display weakness in reflecting cultural factors, particularly political issues related to culture. This evidence from elsewhere was also reflected by the interviewees:

I believed that the management level is the most important level amongst the firm structure … However, some managers have different types of mentalities that could affect the corporate governance rules by crossing some rules … this in turn will definitely lead to the influence of the firm performance level based on the manager’s mentalities. (GM, Firm 2, High)

Cultural factors, such as language and education, are considered to be one of the most important issues that directly impact the level of firm management performance … I think that religion does not have any effect on the corporate governance and firm performance at all … since we are in this country, which has a great understanding that each one can believe as he/she needs. (FM, Firm 1, High)

### 7.4.2 Religion

The interviews revealed that religion was potentially of moderate consideration in the corporate governance – firm performance relationship in Kuwait and this was then investigated further. As shown in Table 7.3, high-performing firms ranked religion
eighth, and sixth in both moderate- and low-performing firms. There is also some support for these results in other studies. For example, using a sample of 32 countries from 2006 to 2010, Kim and Daniel (2016) documented that strong corporate governance related to Protestantism, even after considering cultural, economic, and legal factors. These results are consistent with sociocultural theory that suggests that religion helps determine the level of agency costs in firms, although Chintrakarn et al. (2017) found that the impact, at least in the US, was only indirect. Elsewhere, Hilary and Hui (2009) argued that religion is important for encouraging employees to support their work, revealing that the religious environment related positively with high levels of firm performance (e.g., \( ROA \) and \( ROE \)). This was also suggested in the interviews.

Religion is great in terms of the people’s behaviour and letting them commitment [sic] to their responsibilities … More religious people is [sic] more effective in getting work done, because they feel that work is a part of their life and that they should do their best to achieve. (FM, Firms 2, Moderate)

However, Nakpodia and Adegbite (2018) and Nakpodia, Shrives, and Sorour (2018) found that of religious, cultural, and political factors, religion had only a weak effect on corporate governance. Most of the interviewees agreed:

I am sure that the religion in this country does not have any impact on firm performance or any other issue … What you believe is between you and your god. (GM, Firm 3, Low)

Religion is important to your life and makes you a straightforward person … But I believe that there is no relationship between corporate governance and religion. (FM, Firm 3, High)

Religion could affect your lifestyle for you to be a good person in your life aspects, your work being one of these aspects … I think there is no association between religion and corporate governance. (GM, Firm 1, High)

7.4.3 Politics\(^6\)

Political issues are another factor that could potentially affect the nature of the relationship between corporate governance and firm performance in Kuwaiti firms. As

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\(^6\) Pettigrew (2014) defined the political process as generation of demands for resources and mobilization of support for the demands generate.
shown, this seemed especially so for moderate-performing firms where political factors ranked first. In related work, Domadenik, Prašnikar, and Svejnar (2016) modelled the influence of political corruption on corporate governance, firm production, and firm efficiency and effectiveness in Slovenia. Their results revealed that firm regulation does not necessarily develop the democratic institutions required to protect firms from political corruption, in turn leading to a reduction in firm performance. In this regard, the interviewees stated:

Some political issues in our firm are leading to unintentional financial corruption; for example, weaknesses in issuing the roles that protect the investors definitely leads to a decrease firm performance. (FM, Firm 1, Moderate)

The main problem that we are dealing with nowadays is political; we are living in the same country, which means that each new decision will affect our firm’s performance. For example, the regularity authorities recommend decreasing our high-quality product prices, which will definitely influence us badly. (BC, Firm 3, Moderate)

In addition, ‘family power’ in firms is another concern when considering political issues that could lead to a reduction in firm performance. For example, Muttakin et al. (2015) found that political connections in Bangladesh were more important in family than non-family firms, which was also suggested in one of the interviews:

The main reason for the decreasing levels of firm performance in developing countries is dominating the family on the firm ownership; therefore, developed countries are less affected from this dilemma since their regulator is based on several issues to reduce any potential political problem. (GM, Firm 3, Low)

More recently, Boateng, Liu, and Brahma (2019) measured the impact of ownership as a moderating variable on the relationship between political connections and risk decisions in China. In terms of the interviews, two statements are relevant:

I believe that the ownership concentration is one of the political connections in some firms, since the power of some families and managements dominate several firms. In my opinion, this issue definitely will lead to more complicated issues to corporate governance … this will lead to issues in new roles that help these people, and then lead to bad firm performance. (GM, Firm 2, Moderate)
More ownership concentration is more likely lead to bad firm evaluation where higher types of ownership relate to several issues, such as new roles to serve groups of people and dominate whole sectors. (GM, Firm 3, High)

In other work, Jackowicz, Kozłowski, and Mielcarz (2014) considered the effects of political connections on firm performance and found that political connections negatively related to operational performance levels and firm profitability. Similarly, Wang et al. (2019) used a sample of Chinese firms to examine the influence of political connections on corporate governance and firm performance, while Wu et al. (2018) focused on the political connections evident in executive compensation strategies in private Chinese firms. There was some suggestion in the interviews of the interface between political connections, family ownership, and firm management, especially relating to human resources:

I think that the new political connections, as well as the development of political relationships with the other countries, are very important to reduce political corruption and increase firm performance and corporate governance … Since such kinds of issues reduce the family ownership control and reduce the networking in the firms to hire non-educated people. (GM, Firm 2, Low)

Using agency theory, Liedong and Rajwani (2018) argued that political ties lessen financial statement quality, board independence, and nonfinancial information disclosure. This argument that strong political ties negatively affect firm performance was also evident in the interviews:

As you know, our cultural attitude affects all our life aspects, and I believe that the political ties and connections have affected our firms in several ways. Some people who have the power sometimes force the firms to hire their relatives, and you know this issue definitely will lead to a reduction in the quality of firms in total, particularly if this person is unqualified. In addition, the roles that were established to organise the firm’s financial and non-financial transactions are weak. (GM, Firm 2, High)

7.4.4 The Tribal System

The tribal system is particularly strong in Kuwait, but also elsewhere in the Middle East and North Africa. The results in Table 7.3 suggest this has little influence on the corporate governance – firm performance relationship, where it ranked only ninth, tenth, and eighth as a factor in high-, moderate- and low-performing firms, respectively. In contrast,
Rowland (2009) concluded that tribal law worked within Arab countries as a way to smooth business relations outside civil law, while Oyedele and Firat (2018) found that tribal rule was one of the main challenges foreign firms encountered in implementing their strategies in emerging markets. In this regard, one interviewee stated:

One of the factors that influence our firm aspects is the tribal system, since it has strong power in our country … Hiring people that are not qualified is one of the common problems that our firms suffer nowadays. (GM, Firm 1, Low)

Using a sample of Saudi Arabian firms, Alshetwi (2017) revealed that when the business structure is dominated by a tribal system it gives more attention to individual and personal associations when choosing both board members and other stakeholders such as employees. Zoogah (2016) examined the impact of tribal diversity on human resource management in Africa, and revealed a negative relationship, which in turn resulted in poor firm performance. The interviewees likewise suggested the strong and enduring effect of the tribal system in Kuwait:

The problem of tribal systems went further than hiring employees … It reached hiring the board of directors and choosing them based on the relationship between the people and their power. (GM, Firm 2, Moderate)

Cordes et al. (2008) also evaluated the impact of tribal systems on firms, concluding that modern firms that go out of their way to avoid or prevent tribalism in their work better than otherwise. The interviewees highlighted this problem in Kuwait and its continuation even under the new corporate governance framework:

I agree that the tribal system is considered to be one of the firm threats that could lead to destroyed firms, not only affecting the firm performance … I hope, from our regulatory authorities that we can establish a law that prevents such kinds of problems in our country. (FM, Firm 1, Moderate)

7.5 Analysis of External Accounting and Financial Factors

7.5.1 International Financial Reporting Standards (IFRS)

Adopting IFRS is an important development that has led to the improvement of business in the last decade throughout the world. As shown in Table 7.3, both high- and low-performing firms consider IFRS adoption to be the second-most important factor affecting the corporate governance – firm performance relationship in Kuwait. In a recent study, Nalukenge, Nkundabanyanga and Ntayi (2018) studied the nature of the
relationship between corporate governance, ethical culture, internal control, and compliance with IFRS in Ugandan microfinance institutions. The results indicated that an increase in the level of IFRS compliance led to an increase in the rate of corporate governance adoption in firms, as well as an increase in the level of cultural ethics. One of the interviewees stated:

IFRS adoption in Kuwait occurred in the beginning of 2016. The business life started to be much better than previous years, before adopting IFRS. As I understood that your study used two methods (quantitative and qualitative) to examine the relationship between corporate governance and firm performance, this meant that the quantitative results after IFRS adoption was better compared with the period before the compulsory adoption of IFRS. I am not saying that from my mind, but from my research experience, as I am a PhD holder in this field. (BC, Firm 1, Low)

IFRS has also likely benefited audit committees as a corporate governance factor relating positively with firm performance. For example, Sellami and Fendri (2017) used several audit committee characteristics, such as audit committee size, independence, meetings, and expertise to examine their impact on the level of IFRS compliance in South Africa. The main finding was that high compliance levels with good audit committee characteristics were more likely to lead to an increase in firm performance levels with the adoption of IFRS. Kouaib, Jarboui, and Mouakhar (2018) revealed that the mandatory adoption of IFRS in the European Union led to an increase in the negative relationship between CFO experience and earnings at the management level. Some of the interviewees also touched on this relation:

In my opinion, audit committees and other committees in firms are playing big roles to maintain the firm’s high-quality performance. Before 2016—before the adoption of IFRS was compulsory—most of our firms did not comply with corporate governance in a good way. I think our firms nowadays are better compared to the period before 2016. (GM, Firms 2, High)

One of the IFRS adoption advantages in our firm was that the CFO started to be separate from the board of directors’ chairperson; this in turn led to better firm performance quality. I hope that our entire firm complies with separating between [the] CFO and chairperson of board directors to have an ideal corporate governance code in our country. (FM, Firm 2, Low)
Samaha and Khlif (2016) used four phases to describe the impact of IFRS on corporate characteristics, regulations, and economic consequences in developing countries: 1) IFRS adoption motivation, 2) IFRS compliance with corporate characteristics, 3) IFRS adoption and economic consequences, and 4) the strength of regulations to control IFRS compliance. Although they found the macroeconomic impact of IFRS adoption was limited within the economic theory of network and isomorphism in developing countries, the results relating to the relationship between the corporate characteristics and the IFRS compliance level were inconclusive. In addition, IFRS had a limited impact on foreign direct investment, the cost of equity, and earnings management. The interviewees provided a similar view:

I agreed that the adoption of IFRS triggered a big growth in our firms, whether in operational or in financial transactions, but I am sure that this growth is still limited, since we have several barriers that prevent our firm from benefitting from IFRS, adoption such as cultural factors and political issues. (GM, Firm 3, High)

IFRS adoption has a limited impact in protecting our foreign investors; I believe this refers to the weakness of the regulations compared to IFRS adoption. (GM, Firm 2, Moderate)

In other work, Ofoegbu and Odoemelam (2018) examined the empirical relationship between disclosure practices under IFRS and firm performance in Nigeria, revealing that the extent of overall disclosure displayed no relationship with firm financial performance. However, there did appear to be a strong indirect effect with the stock price, firm size, audit firm size, leverage, and firm age all affecting the disclosure of firms. The interviewees seemed to agree:

We believe that the adoption of IFRS in developed countries and second-world countries has more impact on business aspects compared to our developing countries; however, we are in Kuwait doing our best to be one of the developed countries in the near future once we have a strong economic growth. (FM, Firm 2, Moderate)

I was working in a Western firm for several years; I found that in developing countries, we still need more improvement to achieve the target of IFRS adoption; in fact, we, in Kuwait, started developing our financial and non-financial system in the firm to be amongst that of developed countries soon. (GM, Firm 2, High)
7.5.2 Financial Crisis

The 2008 global financial crisis resulted in the collapse of a large number of financial firms around the world, with governments supporting some of these firms in order to reduce the restriction of global credit markets (Erkens, Hung, & Matos, 2012). The financial crisis remained strong in the memories of the interviewees as it ranked as either the fourth or fifth most important factor affecting the corporate governance–firm performance relationship in Kuwait. In terms of nonfinancial firms, in a Korean study, Joe, Jung, and Oh (2019) suggested that owner-manager firms performed significantly better than those with employed managers. Some of the interviewees were positive about the impact of the most recent financial crisis on their firms in terms of eliminating some foreign firms and encouraging Kuwaitis to look outside its borders:

You might say that I am strange in this point, but I found that the financial crisis presented to the Kuwait market a big gift by cleaning the Kuwait market from [sic] fake firms, particularly foreign firms, that were aiming to benefit from the strength of the growing Kuwait economy. (FM, Firm 1, Moderate)

I think the financial crisis allowed us, as Kuwaiti firms, to sign new agreements with big firms around the world to overcome the impacts that have resulted from the financial crisis in 2008; for example, the Alshaya firm built a huge mall that included most of the market names around the world—I can say that the entire world’s brand names are in the Avenues Mall. (FM, Firm 2, Low)

Others pointed to the negative consequences for a still developing economy:

The financial crisis definitely affected our market, since big firms such as Nokia and Motorola finished their work in Kuwait and kept their agencies. (GM, Firm 2, High)

After the financial crisis, our banks started restricting loan processes for firms; this definitely affected us negatively in our firm liquidity; accordingly, several growing firms were closed, since we expected them to be from the best firms in our country. (BC, Firm 3, High)

The worst thing that we have faced after the financial crisis was decreasing the level of our customers, which affected us negatively on our level of profit. The customers had a shortage of income since the financial crisis [that] affected the entire world; in addition, this also affected the ownership concentration, whether
government ownership, family ownership, or managerial ownership. (GM, Firm 3, High)

Several studies conducted throughout the world have highlighted similar issues in other countries. Salehi et al. (2017) revealed that Australian firms with a high proportion of family ownership performed better than non-family firms, while Notta and Vlachvei (2014) discussed the impact of the financial crisis on Greek dairy firm performance, showing that firms with a large market share and loyal customers exhibited positive firm performance, both before and during the crisis. Balachandran and Williams (2018) concluded that the impact of the financial crisis depended on the circumstances (e.g. culture, economics, politics) in each country, while Khodavandloo, Zakaria, and Nassir (2017) concluded that the financial crisis had a generally negative effect on Malaysian firms via the capital structure. Other studies have also examined the impact of the financial crisis on audit committees, with Aldamen et al. (2012) finding that smaller audit committees and audit chair turnover positively related to firm performance. Ezzine (2018) discussed similar issues relating to the size of board and audit committees in French and Saudi Arabian firms during the financial crisis. The interviewees stated:

I am definitely in agreement that a large number of board of directors is more likely lead to more controlling and mentoring in our firms; this in turn led also to the choice of the best committee in our firms, like the audit committee and compensation committee. (BC, Firm 1, Low)

A large number of board of directors in our firm mostly better compares to small board of directors, since we believe in less board of directors in the developing countries due to the fact that we believe that they dominate the firms. (FM, Firm 1, High)

Other studies have highlighted this paradoxical relationship between board size and firm performance, including Reeh and Sharif (2018) in Ireland and Spain. Lastly, Orazalin and Mahmood (2019) concluded that corporate governance, and with it, firm performance, generally improved through need during times of crisis, as also reflected in the interviews for this study.
7.6 Internal Managerial and Accounting Factors

7.6.1 Managerial Incentives and Remuneration

Corporate governance clearly affects the way managers are remunerated and incentivised. This is important, given Rezaei (2012) revealed that incentives positively affect managers, and thereby firm performance, but negatively affect this through providing an incentive for earnings management. Moreover, like political factors and the tribal system, the interviewees in low-performing firms identified managerial incentives and remuneration as a relatively important factor affecting the corporate governance – firm performance relationship among the three firm performance categories, as shown in Table 7.3. The interviewees stated:

Managers’ incentives are considered to be one of the big obstacles that we are dealing with nowadays, not only in Kuwait, but in whole [in] the firms around the world. Seriously, you do not know how the managers manage the firm revenues and expenses to achieve personal motivations, which negatively impacts firm performance since the financial statement does not reflect the real numbers.

(BC, Firm 3, High)

I believe that the managers always work in order to achieve the shareholders’ target, since most of our motivations are to positively impact our firm assessment.

(GM, Firm 2, Moderate)

Habib and Ljungqvist (2005) used a sample of US firms to investigate the impact of manager motivations on firm performance and found that while managers had many options to achieve their incentives in firms, there was insufficient evidence that this actually affected firm risk and return. Bushman, Dai, and Zhang (2015) used pay performance sensitivities to evaluate firm performance, finding that firm performance was increasing (decreasing) in the residual when the dispersion of these sensitivities was too low (high). The suggestion of high agency costs in firms through managers distorting their incentives was also evident in the interviews:

We can say that the main incentives that the managers used were to increase their bonuses and compensations in the firms, but they ignored that this issue could lead to bad effects in their firm evaluations, which will definitely affect their positions in the future.

(GM, Firm 2, Moderate; GM, Firm 3, High; GM, Firm 1, Low)
The managers think that increasing shareholders’ wealth in an unclear way will lead to affecting the firms negatively; for example, the financial statements are not correct, so all their decisions are incorrect. (BC, Firm 3, High)

Increasing the profit through manipulating revenues and expenses in order to attract more foreign investors is considered one of the worst scenarios that the manager used after the financial crisis; in my opinion, using such scenarios is negatively impacting the firm’s future decisions. (FM, Firm 1, Moderate)

### 7.6.2 Accounting Systems

Lastly, the interviews highlighted some concerns about the differences in accounting systems in Kuwait, even though this was referenced least of all of the ten sub-themes across all firm performance categories, and only ranked tenth in importance by high- and low-performing firms, but was fourth for moderate-performing firms. Some, especially larger foreign firms, employed what they referred to as ‘advanced’ or ‘modern’ accounting systems, including accounting software programs, such as QuickBooks, ERP, and Oracle, to record their transactions. In this regard, the interviewees stated:

> I respect all the firms, whether local or foreign, that used the advanced level of the accounting software system in order to organise all the firm transactions.’
> (BC, Firm 3, High)

> I can divide our firms into two methods according to the accounting systems in Kuwait: the advanced accounting system method (these firms are considered to be big firms, whether local and foreign), and the second one is the traditional accounting system method, which is implemented in medium- and small-sized firms, particularly local firms since medium foreign firms are sometimes to be from advanced accounting system methods. (FM, Firm 1, High)

> All firms that use the advanced level of accounting software programme, such as QuickBooks, ERP, and Oracle are considered as modern and advanced firms in Kuwait, since using such kinds of programmes leads to heightened firm performance quality compared to the firms that used the weak accounting software programme … I do not want to say the name of these programmes. (FM, Firm 2, Moderate)

Others referred to the ‘traditional’ accounting systems used by mostly smaller and local Kuwaiti firms with unknown accounting software:
I think that up to 60% of our local Kuwaiti firms are following the traditional accounting system. (GM, Firm 2, High)

I hope that all our firms in Kuwait follow the advanced level of accounting system. Unfortunately, a large number of firms are still using the old-fashioned accounting system by using unknown accounting software systems (FM, Firm 1, High)

Most of the firms that are following the traditional accounting system method are local and use unknown software accounting systems. I think if we keep adopting this method, then our economy will decrease. (GM, Firm 2, Moderate)

Based on these responses, the lack of development in accounting systems remains a major challenge to many Kuwaiti firms.

7.7 Conclusion

Conventionally, quantitative methods serve to evaluate the corporate governance – firm performance relationship. In this paper, the findings show that this may yield results subject to significant bias from underspecified models, a lack of proxies for corporate governance variables, and the limited availability of suitable data. This is particularly the case in the chosen context of Kuwait, where recent, rapid, and extensive corporate governance reform seemingly defies parametrisation. The qualitative methods used here should provide insights into corporate governance, management decision-making, and firm performance not possible using quantitative methods. A wide range of sub-themes relevant to these main themes in the analysis were discussed, including the role of cultural factors such as religion and tribal systems, economic and political circumstances, government regulations, financial crises, the transformation of accounting systems, and the adoption of IFRS.

As expected, the findings revealed many interesting insights into the corporate governance – firm performance relationship not obtainable though quantitative analysis. However, significant differences were also identified across Kuwaiti firms. Overall, high-performing firms seem much more focused on higher-order factors such as corporate governance reform, the role of the CMA, IFRS adoption, and the 2008 financial crisis, and their impact in the past and the future. In contrast, both moderate- and low-performing firms emphasise the role of culture, religion, politics, and the tribal system in modifying
this relationship and appear to struggle with elements concerning managerial incentives and remuneration and accounting systems. This poses important implications for managers, boards, regulators, and investors. For example, large numbers of our board of directors are government and family shareholders, which could, in turn, cause a conflict of interest between shareholders and managers. Several motivations for managers were explored to achieve their personal objectives that related to government regulation and firm transactions, such as increasing their bonuses and compensations, increasing shareholders’ wealth, and attracting foreign investors to our markets—particularly after leaving several investors during the financial crisis. In addition, utilising the way of employing agency and sociocultural theories in corporate governance and firm performance issues, and how they affected the relationship between these two issues, is important for managers and boards to understand the relationship in their firms’ parties.

The cultural factors recognised by our analysis, such as the networking and tribal systems in Kuwait, seemingly have negative effects on the firms’ performance in several ways, such as the recruitment decisions, which results in people being employed to roles for which they do not have the qualifications or experience. This might result in managers who are not qualified to question the board of directors and, in addition, could result in more errors and manipulations in the financial reporting. The networking and tribal systems also affect the efficiency of business operations.

Of course, there are several limitations of this analysis. One challenge was the time required for the interviews, translating Arabic to English, and obtaining an accurate interpretation of the intended meaning conveyed by the interviewees. This was a very time-consuming process and necessarily limited the size of the sample. Another problem was that despite the best assurances of the interviewers regarding the confidentiality of the process as dictated by extensive formal ethical approval, many interviewees were concerned that their responses may inadvertently divulge sensitive information, harming possibly both their firm and their own careers. One consequence might be that they provided information that was somewhat less forthright than ideal.
Chapter 8: Conclusion

8.1 Thesis Summary

This thesis investigated corporate governance and firm performance in Kuwaiti industrial and services firms. Chapter 1 introduced the thesis by discussing the relationship between corporate governance and firm performance, detailing the current understanding of corporate governance and firm performance in Kuwaiti industrial and services firms, as well as providing a brief explanation of the variables used to proxy the quality of corporate governance and firm performance in the empirical part of the thesis. The chapter also explained the motivation for the thesis in relation to corporate governance both internationally and in Kuwait in particular. Lastly, the chapter presented the four major research questions addressed by the thesis. These compromised three separate questions on the role that firms’ boards of directors, audit committees, and ownership structure play as key parts of corporate governance frameworks in determining firm performance, and an additional question on the role—if any—that cultural, social, political, and economic circumstances play in modifying the relationship between corporate governance and Kuwaiti firm performance.

Chapter 2 provided the institutional and regulatory background of the thesis, comprising a brief discussion of Kuwait’s recent economic and social development, including how these could potentially affect the causal relationship between corporate governance and firm performance. The chapter also covered the history of Kuwait and the Kuwaiti Stock Exchange as a further way to improve understanding of the thesis context. This was particularly relevant when considering how the different corporate governance regulations affect the comparison of studies undertaken in different national contexts. The chapter concluded by exploring the corporate governance mechanisms in Kuwait and other Gulf Cooperation Council countries as a means of drawing a comparison with the corporate governance codes in other closely related countries.

Chapter 3 reviewed the three primary extant theories relevant to the topic of corporate governance, namely, agency theory, stakeholder theory, and institutional theory. First, agency theory is a principle used to explain and resolve issues in the relationship between principals and their agents. In the chosen context, this relationship is between
shareholders, as principals, and company executives, as agents, and arises due to the separation of ownership and control in public companies. This theory helped to define the optimal relationship between corporate governance and firm performance and to show how agency conflicts in this setting can potentially affect the conduct of good corporate governance.

Second, stakeholder theory states that firms have relationships with parties other than shareholders, customers, employees, government, and suppliers. This helped with understanding where corporate governance fits more broadly in promoting firm performance. Lastly, institutional theory concerns deeper and more resilient aspects of social structure that affect business behaviour. It considers the processes by which structures, rules, norms, and routines establish authoritative guidelines for social behaviour. This was used to understand the cultural variables, legal system, and political circumstances that affect the corporate governance – firm performance relationship. The chapter concluded by proposing the theoretical model used for evaluating corporate governance and its relation to firm performance throughout the remainder of the thesis.

Chapter 4 provided a comprehensive review of the extant empirical research concerning the relationship between corporate governance and firm performance. The chapter examined not only the different aspects of corporate governance and how these can be measured in a real-world context, but also firm performance. Particular attention was paid to the findings of existing studies and the methodologies used to obtain these findings. For the most part, the prior literature measured the empirical relationship between corporate governance and firm performance using quantitative methods, but the potential for qualitative methods to provide detailed insights was also discussed.

Chapters 5, 6, and 7 provided the empirical component of the thesis. Using the contextual considerations in Chapter 2, the theoretical framework in Chapter 3 and the literature review in Chapter 4, Chapters 5 and 6 employed unbalanced panel data for between 61 and 95 Kuwaiti industrial and service firms operating over the period 2010–2017 to investigate the impact of corporate governance, and its reform, on firm performance. Chapter 5 began by responding to the first research question concerning the relationship between ownership structure as a key part of corporate governance and alternative firm performance proxies, namely, the return-on-assets (ROA), return-on-equity (ROE), and Tobin’s Q (TQ) in Kuwaiti industrial and services industrial firms. The use of a range of
alternative but related performance measures yielded greater insights than possible in analysis using only one or two measures, as is common in existing work.

The chapter revealed that, of the four types of ownership included in the analysis, family ownership had the most significant impact on firm performance, both in terms of individual firms and at the market level, given the relatively high level of family ownership in Kuwaiti listed firms. In addition, institutional local ownership had a high and positive relationship with firm performance proxies $ROA$, $ROE$, and $TQ$, which may reflect their familiarity with the local investment market.

Last, government ownership, while generally relatively small in share (less than family or institutional local ownership, but more than institutional foreign ownership), appeared influential in increasing the level of firm performance in firms. The findings also suggest that the corporate governance code reforms that have attracted so much attention in Kuwait and in neighbouring markets appear to have had little impact on firm performance. As the reforms are clearly significant as written in terms of their potential impact, this could indicate that most firms already met these guidelines prior to their implementation and that therefore that the reforms were generally not required.

Chapter 6 responded to the second and third research questions centring on the relationship between the characteristics of boards of directors and audit committees as proxies for the quality for corporate governance and firm performance as variously measured for Kuwaiti industrial and services firms over the period 2010–2017. The period selected was particularly interesting as it corresponded to the staggered implementation of Kuwait’s new corporate governance code and guidelines, with the expectation that these would significantly improve corporate governance in the country, and with it, listed firm performance.

The results showed that board size was positively related to firm performance, as expected, particularly with $TQ$. In addition, the proportion of independent board members positively related to firm performance proxies $ROA$, $ROE$, and $TQ$, and the proportion of board outsiders only to the returns on assets and equity.

As for audit committee characteristics, only audit committee expertise related to firm performance. Further, the sign on the estimated coefficient for committee size did not correspond with the hypothesis of a positive relationship with firm performance. One possibility is that too large a committee is ungainly and unable to effectively perform its
role of supervision and risk assessment. Another possible is that the proxies used for the quality of the audit committee vis-a-vis good corporate governance, while well established in the literature, do not actually do a very good job of explaining firm performance.

Finally, Chapter 7 responded to the fourth research question using a semi-structured interview approach as a qualitative method. This chapter detailed in-person interviews with 14 managers (six general managers, five financial managers, and three board of directors’ chairpersons) in nine Kuwaiti industrial and services firms. Of these nine firms, three displayed high positive firm performance, three firms had high negative firm performance results, and three firms had low negative or positive firm performance results. The interviews ranged from 35 minutes to 75 minutes. All interviewees were highly qualified and experienced and were therefore able to provide useful insights into corporate governance in Kuwait.

The results indicated that cultural, political, economic, governmental, and financial circumstances in Kuwait all played a key role in moderating the role and potential impact of the corporate governance mechanism in Kuwaiti firms. The chapter also revealed that the adoption of IFRS was critical when it came to firms’ compliance with the new regulations. However, several of the respondents noted that it had been difficult for their firms to comply with the new corporate governance code and maintain good performance during the sample period.

### 8.2 Thesis Contribution

This study contributes to the corporate governance literature in three main ways. First, it provides detailed insights into how contextual factors in a given country’s corporate governance system—including the tribal system, culture, and history—influences the development of a suitable corporate governance framework. While there are universally agreed principles of corporate governance, in reality it is not always possible to implement easily in a particular context, especially in developing markets. In the case of Kuwait, the Middle East revolutions and their impact on the oil market, and the broader position of Kuwait among the GCC and in the Middle East and North Africa, are key to understanding how corporate governance reform works in practice.

Second, one major limitation of existing empirical studies is that they were conducted during largely stable periods with little institutional and regulatory reform. Given that this
thesis was set in Kuwait, a small but influential market undergoing rapid regulatory change, it was possible consider the corporate governance–firm performance relationship across three separate institutional and regulatory regimes: a pre-corporate governance code regime, a voluntary corporate governance regime, and a compulsory corporate governance code regime. This permitted valuable insights into how corporate governance developments outside the firm affect the firm. At the same time, a mixed methods approach comprising both conventional quantitative methods and a much less common qualitative method allowed a more detailed and insightful inquiry into the mechanism by which corporate governance and its reform affect firms and their performance.

Third, the thesis also makes a strong contribution in that it considers the corporate governance–firm performance relationship in the context of a developing market. Most existing studies have only considered large and mature developed markets, primarily the USA and UK, and only a few have analysed developing markets. This is interesting, in that only in these markets will pertinent considerations like government, family, and institutional ownership all come to the fore, leading to results that are directly of benefit to several parties, including (but not limited to) decision-makers, regulators, investors, and senior managers. The thesis also considers corporate governance in its broadest possible perspective, with insights not only for institutional and regulatory change, but also for accounting and management practice.

8.3 Implications for Industry Policy and Practice

The findings in this thesis provide three main implications for industry policy and practice. First, the thesis provides useful insights into corporate governance policymaking in Kuwait. In particular, the findings reveal the success of the corporate governance code and changes to capital market regulation and how they have improved both the conduct of corporate governance and the quality of listed firms on the Kuwait Stock Exchange. This will equip regulators with the required justification to force all Kuwaiti industrial and services firms to adopt IFRS immediately, and to further reform the corporate governance regime in Kuwait. In addition, it will help increase the ability of the Kuwait Capital Markets Authority to develop and improve firm-level regulations and policies.

Second, the empirical findings highlight the importance of independent boards by helping the decision-makers, regulators, investors, and managers to enhance corporate quality. In
addition, audit committee characteristics are judged an essential tool in improving and developing the business environment—whether in developed or developing countries. Last, the provision of complete accounting information is an important input in ensuring improved financial reporting quality. This suggests that firms, both in Kuwait and elsewhere, are well justified in continuing to strengthen the independence of their boards, ensuring the professionalism and the conduct of their audit committees, and continuing to develop the quality of their accounting information.

Third, the findings also identified several factors that may potentially hinder the success of corporate governance reforms in developing markets. In Kuwait, the traditional tribal system was found to continue to dominate the mentality of policy decision-makers through the power of the tribal chairperson. Political circumstances may also limit the quality of corporate governance reform, whereby decision-makers continue to focus on these rather than on objectively developing and improving code, regulations, and legislation. Of note are the recent revolutions in the Middle East. Additionally, efforts need to be made to ensure that firms continue to incorporate good corporate governance processes and practices within themselves. This suggests a proactive and ongoing role for regulators, investors, management, and boards, and will benefit firms, in terms of attracting investment capital, enhancing corporate performance, and reducing investor risk, and the market through industrial production, employment, and growth.

8.4 Thesis Limitations

This thesis has several limitations. The first relates to the availability of data and the specification of the variables and models. To start, given its stage of economic and financial development, many of the requisite annual financial reports for Kuwaiti firms do not exist within the DataStream database, and this potentially qualifies some of the findings, particularly if they result from self-selection or systematically include one or more industries or types of firms. In addition, the governance mechanism within Kuwait is both internal and external; however, this thesis focused largely on the former. Likewise, the specification of ownership structure was limited, being confined to only family, institutional, and government ownership, and it may well have been interesting to investigate some of the several different ways ownership could be specified beyond simply the proportion of shares owned and controlled. Overall, notwithstanding the benefits of focusing on Kuwait, as a single-country study, especially one conducted in a
development market context, there is an explicit limitation in terms of the generalisability of the results.

Second, it was exceptionally difficult to conduct the structured interviews. All of the interviewees were non-native English speakers, which necessitated translating their responses from Arabic into English. It is possible that this resulted in some misunderstanding or misinterpretation. It was also difficult to convince interviewees to allow the researcher to record the interviews in the first place, as they held legitimate concerns, despite the assurances of the official ethical approval process, about whether the results would be used to exploit firm information that could potentially impact upon their own careers. Even when they did agree to participate, it is possible that they were guarded or restrained in their responses. Some of the interviewees even vocalised their fear that discussing the operational and financial position of the firm could lead to them their losing their job. Hence, the responses collected may have painted the firms in a rather more positive light. A wider sample of interviewees may have addressed some of this possible bias.

Third, each interviewee was questioned in different ways, which could have influenced the results drastically and this often led to interviewees slightly altering their answers, presumably in the hope of giving the ‘right’ one. These alterations could also have occurred as a result of interviewing people who have different cultural, academic, and reputational backgrounds, as these will have understandably influenced how a given employee would want to come across. Additionally, it may simply be that a given interviewee had an unstable grasp on some of the knowledge they were being questioned about, and so altered their responses in the hope of reaching a more accurate one.

### 8.5 Directions for Future Research

There are three possible future directions of research that flow from this thesis. First, the sample period was divided into three: a pre-corporate governance code reform period from 2010 to 2012, a voluntary corporate governance code period from 2013 to 2015, and a compulsory corporate governance code period from 2016 to 2017. This provided important support regarding knowledge of corporate governance and firm performance within Kuwait. However, it would obviously be useful to extend the sample period as more and more detailed firm-level information comes to hand. In addition, this thesis considered only industrial and services sector firms and it would be useful to extend a
similar analysis to banking and other financial firms in Kuwait. An additional area for potential research concerns investigating links between the social, economic, and environmental capability of a given firm and its corporate governance. In particular, it would be interesting to consider the interface between corporate social responsibility and corporate governance in Kuwait.

Second, the number of firm-level variables used in this thesis is very limited. Regrettably, this flows from the limited information made available in Kuwait prior to the recent capital market and accounting reforms. Nonetheless, this is expected to continue to improve over time, which will allow a reassessment of the findings in this seminal analysis. One benefit of lengthening and widening the firm-level data available is that it will be possible to consider the robustness of the findings in thesis, limited in part through limited unbalanced and balanced panels, and possibly survivorship bias. Related to this, it would be ideal if future research could include several other GCC countries, particularly given the similarity in geographic, economic, and cultural contexts, and the wide range of approaches to corporate governance reform over time.

Third, one of the most important results from the detailed semi-structured interviews is that they disclosed a range of external cultural factors (especially religion, the tribal system, and the Kuwaiti monarchy) that seemingly affect both business regulation and conduct in Kuwait. This is also the case in other economies in the Middle East. It would be very interesting to investigate this further, although this may not be possible using conventional corporate finance research techniques, and would instead need to draw upon cross-disciplinary insights from fields such as sociology and politics.


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Larcker, D. F., Richardson, S. A., & Tuna, A. (2005). *How important is corporate governance?* Available at SSRN 595821


References


### Appendices

#### Appendix (1)

Regression Robustness Estimates for All Models

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Note: Asterisks denote significance at the *** – 0.01, ** – 0.05, and * – 0.10 level.

### Appendix (2)

**Regression estimates (OLS, GLS, and Fixed Effects)**

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### Fixed effects regression

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Note: Asterisks denote significance at the *** – 0.01, ** – 0.05, and * – 0.10 level.
To Whom It May Concern

Human Research Ethics Approval
“Corporate Governance and Firm Performance in Kuwait”
(Ref: 2017/903)

I am pleased to advise that this research has approval to commence from the Griffith University Human Research Ethics Committee, a committee established and operating in accordance with the standards and principles of the Australian National Statement on Ethical Conduct in Human Research (2007) and Griffith University policy.

The decision to approve is dated 22 November 2017 and covers the period 22 November 2017 to 10 July 2020.

For any queries regarding this ethical approval please contact the Committee Secretary on tel: 07 3735 4375 or research-ethics@griffith.edu.au.

Yours sincerely,

Rick Williams
Secretary to the Griffith University
Human Research Ethics Committee and
Manager, Research Ethics and Integrity
Office for Research
Griffith University
Nathan Qld 4111 Australia

24 November 2017